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TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1938

No. 304

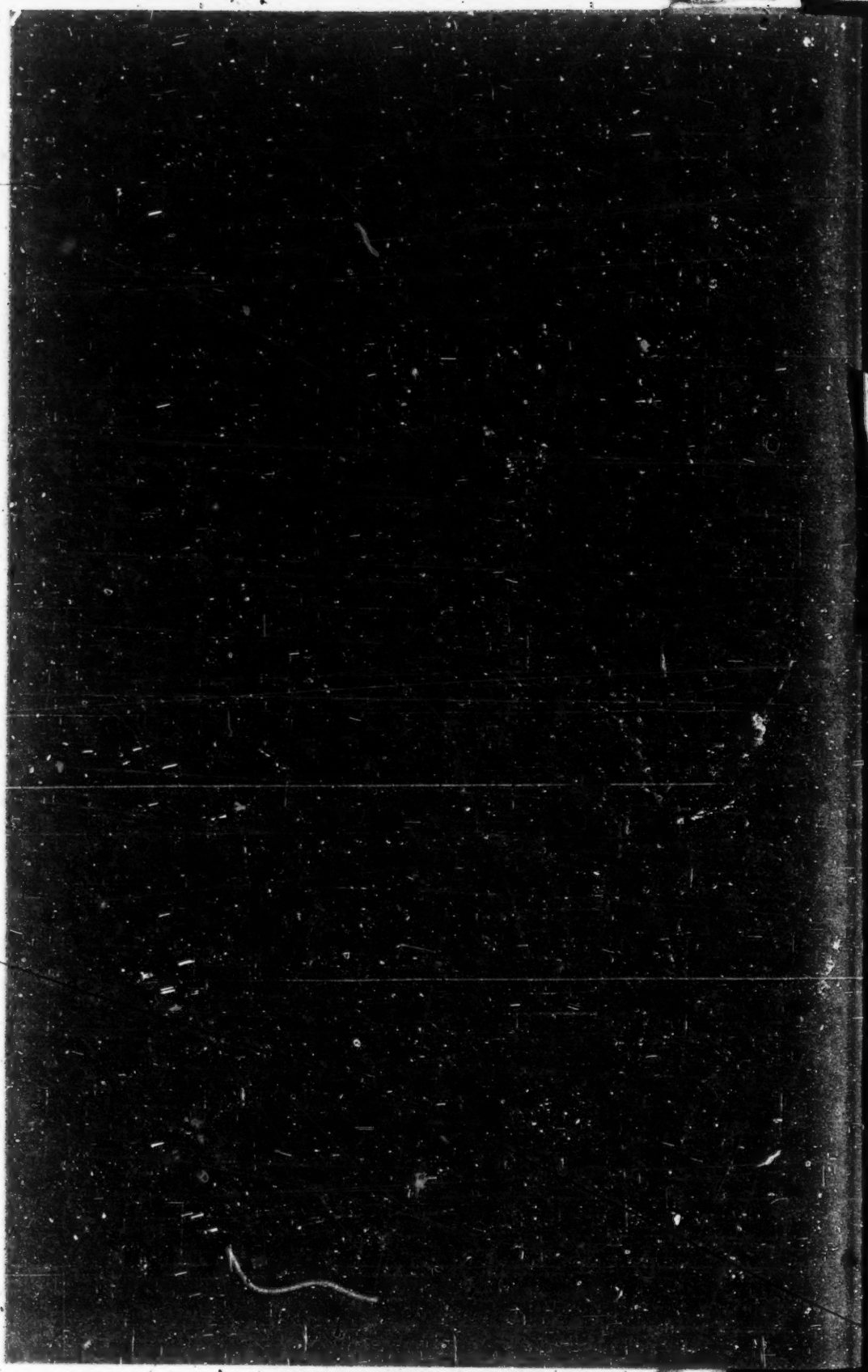
GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

CHESTER N. WEAVER COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR CERTIORARI FILED AUGUST 26, 1938
CERTIORARI GRANTED OCTOBER 10, 1938



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104469—38

APPEARANCES:

For Taxpayer:

ADOLPHUS E. GRAUPNER,
ARTHUR E. COOLEY, Esq.

For Comm'r:

O. W. SWECKER, Esq.
Transferred to Mr. Turner 11/20/36.

Docket No. 82865

CHESTER N. WEAVER CO. a corporation.
Petitioner.

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES.

1936

Feb. 4—Petition received and filed. Taxpayer notified. (Fee paid).

Feb. 5—Copy of petition served on General Counsel.

Mar. 24—Answer filed by General Counsel.

Mar. 26—Copy of answer served on taxpayer.

May 8—Hearing set week of 7-6-36 at San Francisco, Calif.

July 6—Hearing had before Mr. C. P. Smith, Div. 5, on the merits. On Counsel's motion 82865, 82870 and 82871 consolidated. Stipulation as to facts filed. Pet's brief due Aug. 6, 1936. Respondent's 9/7/36. Reply due Oct. 7, 1936.

July 27—Brief filed by taxpayer. 7/28/36 copy served.

July 31—Transcript of hearing July 6, 1936, filed.

Sept. 18—Motion for leave to Sept. 19, 1936 to file brief, filed by General Counsel. Brief lodged. 9/18/36 Granted.

Oct. 19—Reply brief filed by taxpayer. 10/19/36 copy served.

1937

Feb. 17—Findings of fact and opinion rendered, Bolon B. Turner, Div. 8. Decision will be entered under Rule 50.

Feb. 27—Motion for decision under rule 50 filed by General Counsel.

Mar. 3—Hearing set March 24, 1937 on settlement.

Mar. 12—Consent to settlement filed by taxpayer.

Mar. 20—Decision entered, Bolon B. Turner, Div. 8.

Apr. 20—Supersedeas bond in the amount of $8,646.96 approved and ordered filed.

Apr. 20—Petition for review by United States Circuit Court of Appeals, Ninth Circuit, with assignments of error filed by taxpayer. Affidavit service of petition for review filed.

Apr. 21—Proof of service filed by taxpayer.
May 24—Praecipe, filed by taxpayer.
May 24—Affidavit of service of praecipe filed.
May 24—Order from Circuit Court of Appeals, 9th Circuit that procedure as stipulated by both parties be adopted—further proceedings in accordance therewith—filed. [1*]

United States Board of Tax Appeals

Docket No. 82865

CHESTER N. WEAVER CO., a corporation,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION.

Without waiver of right to challenge the constitutionality of any part of any Revenue Act involved in this proceeding or any act of the Commissioner of Internal Revenue or his subordinates or to object to the jurisdiction of this Board, the above named petitioner hereby petitions for a redetermination of the alleged deficiency set forth by the Commissioner of Internal Revenue in his purported notice of deficiency (IT:AR:E-4, GCD-

*Page numbering appearing at the foot of page of original certified Transcript of Record.

90D) dated December 30, 1935, and as a basis of this proceeding alleges as follows:

1. The petitioner is a corporation duly organized and existing under the laws of the State of California with its principal place of business at 516 Sutter Street, City and County of San Francisco, State of California.

2. The purported notice of deficiency upon which this petition is based (a copy of which is hereunto attached and marked Exhibit A) was apparently mailed to the petitioner on December [2] 30, 1930.

3. The asserted deficiency in tax here in controversy is for alleged income taxes for the calendar year 1933 and, as asserted in said purported deficiency notice, in the amount of not more than $4,323.48.

4. The alleged determination of tax set forth in said purported notice of deficiency is erroneous in each and every of the following particulars assigned as errors:

(a) The Commissioner erred in determining and asserting any amount as a deficiency in income tax against petitioner for the calendar taxable year 1933.

(b) The Commissioner erred in increasing in any way the net income reported by petitioner in its income tax return for the calendar taxable year 1933 and in making any reductions from the net income reported by petitioner in said return for said year.

(c) The Commissioner erred in treating as taxable income and disallowing items of reserve in the amount of $3,328.49 which petitioner had set up and maintained on its books of account as a regular and necessary part of its accounting system.

(d) The Commissioner erred in disallowing the amount of $86,859.75 deducted by petitioner from gross income reported in its income tax return for the taxable year herein involved as a loss sustained *though* the dissolution of the Jeff R. Townsend Co., Inc., a corporation.

(e) The Commissioner erred in disallowing the amount of $6,163.04 deducted by petitioner from income reported in its income tax return for the taxable year herein involved as depreciation on [3] certain buildings, office furniture and equipment, machinery and machine shop equipment, and automobiles employed and used by petitioner in the conduct of its business during said taxable year.

(f) The Commissioner erred in disallowing the amount of $56.00 deducted by petitioner from income reported in its income tax return for the taxable year herein involved as depreciation on a fence located on business property in Oakland, California, and owned by petitioner.

5. The facts upon which the petitioner relies as a basis for this proceeding are as follows:

(a)—During the taxable year 1933 herein involved petitioner was engaged in the business of buying, selling, repairing and servicing automobiles, in making investments in stocks and securi-

ties of other corporations and in obligations of the United States and of States and political subdivisions thereof, and in maintaining and operating real property.

(b)—That petitioner had established in its books of account the reserve method of treating various items of expected and anticipated losses and expenses and particularly had established and set up for the taxable year involved a reserve for repossession of automobiles sold on the installment basis in the amount of $3,012.60 and a reserve for insurance in the amount of $315.89. In its income tax return for the taxable year involved the petitioner deducted the amounts of said reserves from its gross income. The respondent denied the deductibility of said items of reserve and added the sum of $3,328.49, representing the amount of said reserves, to petitioner's txable net income.

(c)—On or about August 9, 1932, petitioner purchased for [4] cash one thousand shares of the preferred stock of the Jeff R. Townsend Co., Inc., having a par value of one hundred dollars per share, and paid therefor the amount of $100,000. Said Jeff R. Townsend Co., Inc. was engaged in the business of buying, selling, repairing and servicing automobiles. In September, 1933, the Jeff R. Townsend Co., Inc. was liquidated and petitioner received from said corporation, as a complete liquidating dividend on dissolution thereof, the amount of $13,140.25 and thereby sustained a loss of $86,859.75 on its investment of $100,000. That petitioner

deducted said amount of $86,859.75 from its gross income reported in its return for the taxable year involved as a loss sustained in the conduct of its business. That respondent disallowed said loss as a deductible item and added the amount thereof to petitioner's taxable net income for said taxable year.

(d)—Petitioner as the owner of various depreciable properties claimed as a deduction for depreciation in its income tax return for the taxable year involved the sum of $20,830.42, which sum was computed at the rates of depreciation returned by petitioner and allowed by respondent for previous taxable years and was reasonable in rate and amount in relation to the age and character of the properties and the purposes for which they were used. That respondent reduced the rates of depreciation claimed and returned by petitioner for the taxable year and disallowed the amount of $6,497.75 as asserted excessive depreciation for said year and added said amount to petitioner's taxable net income for said year.

(e)—Petitioner's income and excess profits tax return for the taxable year herein involved disclosed a net loss of $64,403.79 and no tax due or payable. By his arbitrary and illegal disallowance [5] of proper deductions and the addition of the sum thereof to petitioner's returned net income, respondent has illegally and erroneously increased petitioner's taxable net income in the sum of $96,407.28 for the taxable year involved and has there-

on illegally and erroneously determined an alleged deficiency in tax against your petitioner for said year in the amount of $4,323.48.

Wherefore, the petitioner prays that this Board may hear the proceeding and determine that there is no deficiency in tax or additional tax due and owing respondent or any other officer or person from petitioner for the taxable year involved and that it grant petitioner such other and further relief as may be meet.

ADOLPHUS E. GRAUPNER
ARTHUR E. COOLEY
Attorneys for Petitioner
1110 Balfour Building
San Francisco, California [6]

State of California
City and County of San Francisco—ss.

Chester N. Weaver, being duly sworn, says that he is the president of the Chester N. Weaver Co., a corporation, the petitioner herein, and that he is duly authorized to verify the foregoing petition; that he has read the foregoing petition and is familiar with the statements contained therein, and that the facts stated are true, except as to those facts stated on information and belief, and those facts he believes to be true.

CHESTER N. WEAVER

Subscribed and sworn to before me this 29th day of January, 1936.

[Seal] DOROTHY H. McLENNAN,
Notary Public in and for the City and County of San Francisco, State of California. My commission expires December 24, 1938. [7]

EXHIBIT A

Dec. 30, 1935.

IT:AN:E-4
GCD-90D
Chester N. Weaver Co.,
516 Sutter Street,
San Francisco, California.

Sirs:

You are advised that the determination of your income tax liability for the taxable year 1933 discloses a deficiency of $4,323.48 as shown in the statement attached.

In accordance with section 272 (a) of the Revenue Act of 1932, as amended by section 501 of the Revenue Act of 1934, notice is hereby given of the deficiency mentioned. Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Wash-

ington, D. C., for the attention of IT:C:P-7. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiency and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,

Commissioner.

By (Signed) CHAS. T. RUSSELL

Deputy Commissioner.

Enclosures:

Statement

Form 870

GCD/TVW-1. [8]

STATEMENT

IT:AR:E-4

GCD-90D

In re Chester N. Weaver Co.,
516 Sutter Street,
San Francisco, California.

Income Tax Liability

Year—1933.

Income Tax Liability—$4,323.48.

Income Tax Assessed—None.

Deficiency—$4,323.48.

The deficiency shown herein is based upon the report prepared by Internal Revenue Agent D. W.

Johnson, dated April 16, 1935, a copy of which was transmitted to you May 8, 1935, and as the result of a conference held in the office of the internal revenue agent in charge, San Francisco, California, September 6, 1935.

Net income shown on return (loss)		($64,403.79)
Add:		
1. Unallowable reserve	$ 3,328.49	
2. Loss on Townsend Company stock not deductible	86,859.75	
3. Excess depreciation	.6,163.04	
4. Depreciation on fence reversed	56.00	
	$96,407.28	
Deduct:		
5. Capital stock tax accrued December 31, 1933	560.00	95,847.28
Adjusted net income		$31,443.49
Income tax at 13¾%		$ 4,323.48
Previously assessed, original, account #856078		None
Deficiency		$ 4,323.48

[9]

Explanation of Changes

1. The following are considered unallowable reserves not deductible from income:

Reserve for repossession	$3,012.60
Reserve for insurance	315.89
Total	$3,328.49

These reserves relate to automobile sold on term contracts which you carry and do not discount. At the time of sale, an estimate of the probable loss

in event of repossession, etc., is credited to the "Reserve for Repossession" and the amount added to the contract sales price in excess of the cash sales price for insurance carried by you is credited to the "Reserve for Insurance."

Since you report income on an accrual basis, it is held that the credits to the above-named "Reserves" represent taxable income, the losses or other charges thereto being deductible. As you did not begin the auto sales business until April, 1933, the "reserves" in question were all set up within the taxable year under consideration. Therefore, the net credit balance of $3,328.49 is adjusted to taxable income.

2. The records of this office show that in 1931 the Jeff R. Townsend Company was organized by Mr. Weaver and other individuals for the purpose of taking over the automobile business of your company; that a portion of your business was sold to the Townsend Company for cash. Your corporation held none of the common or voting stock of the Jeff R. Townsend Company, but on August 9, 1932, purchased 1,000 shares of its preferred stock for $100,000.00. On March 20, 1933 a resolution was passed by your company to sell the automobile stock and business of the Townsend Company to your company, and on March 28, 1933 a resolution was passed to take the necessary steps to dissolve the Jeff R. Townsend Company. This was finally effected by a sale on September 15, 1933 of the remaining assets, chiefly cash and minor accounts.

The liquidation took place on September 16, 1933 and you received the sum of $13,140.25 as a liquidating dividend, resulting in a loss in the amount of $86,859.75. A deduction in this amount was taken on your return, which was disallowed by the revenue agent in his report covering the examination thereof. [10]

The disallowance was made upon the authority of section 23(r) of the Revenue Act of 1932 for the reason that you had no gain from sales or exchanges of assets held less than two years, and the loss sustained in connection with the stock is held to be from an exchange of stock held less than two years. Section 115(c) of the Revenue Act of 1932 is given as authority for holding that a transaction involving the liquidation of a corporation is to be treated as an exchange.

Section 23(r) of the Revenue Act of 1932 limits the deduction for stock losses and provides as follows:

> "Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations)."

Section 111(c) of the Revenue Act of 1932 which refers to recognition of gain or loss, contains no reference to section 23(r) and contains provisions

relative to sales and exchanges which are similar to those found in section 115(c) relative to distributions in liquidation. See below.

> "Recognition of gain or loss—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purpose of this title, shall be determined under the provisions of section 112."

In transactions coming under the provisions of section 115(c) or 111(c) the deduction for losses is allowable only as provided in section 23(e) which relates to the deduction to be allowed to an individual in computing net income. This section provides for the allowance of certain losses, subject to the limitation provided in section 23(r).

The report of the examining agent has been sustained relative to the disallowance of the loss in the amount of $86,595.75 arising because of the liquidation of the Jeff R. Townsend Company upon the grounds that a transaction involving a distribution in liquidation is to be treated as an exchange and that the limitation set forth in section 23(r) of the Revenue Act of 1932 applies to such transactions.

[11]

3. For details of depreciation, see copy of exhibit attached.

4. Depreciation on fence not deducted on the books restored to income.

5. Capital stock tax not accrued at December 31, 1933 is deductible on the basis of the following computation:

Declared value of capital stock January 1, 1932			$800,990.00
Surplus per books December 31, 1932		$489,000.29	
Surplus December 31, 1933		234,959.34	
Decrease in 1933		$254,040.95	
Less:			
Adjustments increasing surplus per schedule #1 herein:			
Unallowable reserves	$6,994.85		
Excessive depreciation	6,497.75	13,492.60	240,548.35
Value capital stock December 31, 1933			$560,441.65
Capital stock tax at $1.00 for each $1,000.00			560.00

In case you agree to the entire amount of the deficiency, please fill in the amount of $4,323.49 on the enclosed form 870 (Waiver of Restrictions) and forward it, properly executed, to the Commissioner of Internal Revenue, Washington, D. C. However, if you do not acquiesce in all of the adjustments making up the deficiency indicated, but would like to stop the accumulation of interest on that part of the deficiency resulting from adjustments to which you agree, please fill out the form 870 inserting therein the amount you desire to have assessed at once. In the event that you agree to only a part of the deficiency indicated, the execution of the form for the agreed portion of the deficiency will not deprive you of your right to petition the United States Board of Tax Appeals for a redetermination of the income tax liability for the year or years to which it relates.

A copy of this letter, together with a copy of the statement, has been mailed to your representative.

Mr. Arthur E. Cooley, 206 Sansome Street, San Francisco, California, in accordance with the authority conferred upon him in the power of attorney executed by you and on file with the Bureau. [12]

Exhibit "D"
Depreciation Schedule

Item	Cost Basis for Depreciation	Estimated Life (Years)	
S. F. Building	$335,321.60	25	$ 9,102.79
Oakland Building	150,620.41	33⅓	4,518.61
Oakland fence	560.00	10	56.00
Office furniture and equipment S. F.	2,420.00		208.00
Office furniture and equipment Oakland	3,999.86		283.69
Machinery and equipment Oakland	3,786.78		280.45
Service cars Oakland	510.00		81.84
S. F. house car	695.66		80.00
Total depreciation allowable			$14,611.38
Total depreciation per books			20,774.42
Excessive depreciation disallowed			$ 6,163.04
Total cost to January 1, 1933			$174,071.29
Less:			
Depreciation allowed to January 1, 1933			23,450.88
Remaining cost January 1, 1933			$150,620.41
Allowable depreciation on basis of an estimated life of approximately 33⅓ years from January 1, 1933 3% of $150,620.41 or			$ 4,518.61
Depreciation allowed in original report			4,183.90
Additional depreciation allowable			$ 334.71

GCD/TVW-1

[Endorsed]: U.S.B.T.A. Filed Feb. 4, 1936. [13]

[Title of Court and Cause.]

ANSWER

Comes now the Commissioner of Internal Revenue, by his attorney, Herman Oliphant, General Counsel for the Department of the Treasury, and for answer to the petition filed by the above-named petitioner admits and denies as follows, to-wit:

1. Admits the allegations contained in paragraph 1 of the petition.

2. Denies that the notice of deficiency upon which the petition is based was mailed to petitioner on December 30, 1930, as alleged in paragraph 2 of the petition. Alleges that the said notice of deficiency was mailed to petitioner on December 30, 1935.

3. Admits that the amount in controversy is for income taxes for the calendar year 1933. Denies the remaining allegations of paragraph 3 of the petition.

4(a) to (f), inc. Denies that the Commissioner erred as alleged in paragraphs 4(a) to (f), inclusive, of the petition.

5(a). Admits that during the taxable year 1933 herein involved petitioner was engaged in the business of buying, selling, repairing and [14] servicing automobiles. Denies the remaining allegations contained in paragraph 5(a) of the petition.

(b). Admits that in its income tax return for the taxable year involved the petitioner deducted the sum of $3,328.49 as so-called reserves from its gross income and that the respondent disallowed the

deduction of the said amount and added the said sum of $3,328.49 to petitioner's taxable net income. Denies the remaining allegations contained in paragraph 5(b) of the petition.

(c). Admits that petitioner deducted the amount of $86,859.75 from its gross income reported in its return for the taxable year involved as a loss alleged to have been sustained on the liquidation of the Jeff R. Townsend Co. Inc.; admits that respondent disallowed said sum of $86,859.75 as a deduction and added the amount to petitioner's taxable net income for the year involved herein. Denies the remaining allegations in paragraph 5(c) of the petition.

(d). Admits that the petitioner claimed as a deduction for depreciation in its income tax return for the taxable year involved the sum of $20,830.42 and further admits that the respondent disallowed a certain portion of the sum thus claimed as a deduction and added the same to petitioner's taxable net income for the year involved herein. Denies the remaining allegations in paragraph 5(d) of the petition.

(e). Admits that petitioner's income and excess profits tax return for the taxable year involved herein disclosed a net loss of $64,403.79 and no tax due or payable. Admits further that respondent [15] has increased petitioner's taxable net income for the year involved herein and has determined a deficiency in tax against the petitioner for the said year. Denies the remaining allegations in paragraph 5(e) of the petition.

Denies generally and specifically each and every allegation set forth in the petition and not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the appeal be denied.

(Signed) HERMAN OLIPHANT
General Counsel for the
Department of the Treasury.

Of Counsel:
JAMES D. HEAD, JR.,
HUGH R. DOWLING,
Special Attorneys,
Bureau of Internal Revenue.

[Endorsed]: U.S.B.T.A. Filed Mar. 24, 1936. [16]

MINUTES OF PROCEEDINGS

United States Board of Tax Appeals

Date, July 5, 1936.
Place, San Francisco, Calif.
Docket No., 82865, 82870, 82871.
Proceeding: Chester N. Weaver Co.—Chester N. Weaver—Elsie S. Weaver.
Assigned to: Hon. C. P. Smith, Division No. 5.
Counsel for Petitioner: A. E. Graupner, Esq., 1110 Balfour Bldg., San Francisco, Calif.
Counsel for Respondent: O. W. Swecker, Esq.
Stenographic Reporter, Payne.
Hearing: CC.
Transcript Ordered: Yes.
On the merits, Yes.

On the motion of counsel to consolidate for hearing.

Ordered: Motion to consolidate granted.

Filed at hearing: Stipulation as to the facts.

Petitioner's brief: August 6, 1936.

Respondent's brief: September 7, 1936. Reply, October 7, 1936.

Witnesses for Petitioner

[Not filled in]

Witnesses for Respondent

[Not filled in]

EXHIBITS

Petitioner's

(Number and Describe)

[Not filled in]

Respondent's

(Letter and Describe)

[Not filled in]

(Signed) CLIFTON N. JACK,

Division Clerk [17]

[Title of Court and Cause.]

FINDINGS OF FACT AND OPINION

Docket Nos. 82865, 82870, 82871. Promulgated February 17, 1937.

The petitioners sustained losses during the taxable year upon liquidation of a corporation in which they owned all of the preferred stock. They had owned the stock for a period of less than two years. No claim is made that they realized gains during the taxable year from the sale of stocks or

bonds which were not capital assets. Held, that the deduction of the loss sustained by each of the petitioners is barred by section 23 (r) (1) of the Revenue Act of 1932.

A. E. Graupner, Esq., for the petitioners.

O. W. Swecker, Esq., for the respondent.

These proceedings, which were consolidated for hearing, involve deficiencies in income tax for the year 1933 as follows:

Petitioner	Docket No.	Deficiency
Chester N. Weaver Co.	82865	$4,323.48
Chester N. Weaver	82870	8,832.43
Elsie S. Weaver	82871	2,447.84

The only question for our determination is whether petitioners, in determining their net income, may deduct the losses sustained by them upon the liquidation of the Jeff R. Townsend Co., in which they held all of the preferred stock. The losses in question were disallowed by the respondent under section 23 (r) of the Revenue Act of 1932.

Other allegations of error are set forth in the petitions, but since no evidence has been offered to sustain them, it will be deemed that they have been waived. The respondent's claim for an increased deficiency in Docket No. 82871 will also be deemed to have been waived by reason of his failure to offer evidence to support it. [18]

FINDINGS OF FACT

The Chester N. Weaver Co., hereinafter referred to as the Weaver Co., is a California corporation. Chester N. Weaver and Elsie S. Weaver are husband and wife and reside in San Francisco, California.

On December 2, 1931, Chester N. Weaver and Elsie S. Weaver purchased 500 shares each of the 6 percent cumulative preferred stock of the Jeff R. Townsend Co., hereinafter referred to as the Townsend Co., paying therefor $100 per share. On August 9, 1932, the Weaver Co. acquired from the same corporation 1,000 shares of its preferred stock at the same price. The 2,000 shares of preferred stock so purchased constituted all of the preferred stock of the Townsend Co. The common stock belonged to other interests. The articles of incorporation provided that in the event of liquidation the holders of preferred stock should be entitled to receive therefor a sum equal to 105 percent of the par value thereof before any amount should be distributed to the holders of the common stock.

Early in 1933 the Townsend Co. became financially involved and unable to continue business. Its stockholders took the necessary steps to effect its dissolution and liquidation. On or about September 17, 1933, it sold all of its assets to the Weaver Co. for $26,280.50. On September 18, 1933, the petitioners in these proceedings, holders of all of the preferred stock of the Townsend Co., sur-

rendered their stock certificates for cancellation and for the purpose of completing liquidation and effecting dissolution of that company. The $26,280.50 received for its assets was distributed in liquidation to the preferred stockholders pro rata. The Weaver Co. received $13,140.25; Chester N. Weaver, $6,570.13, and Elsie S. Weaver, $6,570.12.

In their income tax returns for 1933 each of the petitioners deducted as a loss the difference between the amount paid for the preferred stock so surrendered and the amount received in liquidation, and, in determining the deficiencies herein, the respondent has disallowed the deductions so claimed.

OPINION.

Turner: The only question for determination is whether or not section 23 (r) (1)[1] of the Revenue Act of 1932 bars the deduction of the losses sustained by the petitioners on liquidation of the Townsend Co. There is no claim by the petitioners that the gross income re- [19] ported, and against which the deduction is sought, includes gains from the sale of stocks or bonds which were not capital assets.

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[1]Sec. 23. (r) Limitation on Stock Losses.—(1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

It is the contention of the petitioners that the provisions of sections 22(d), 115(c), 111, and 112(a)[2] of the act provide for the deduction in full of losses sustained as the result of a distribution in complete liquidation of a corporation, and that the provisions of section 23, relating to deductions from gross income, are not applicable.

The petitioners' argument that the losses in question are deductible without regard to section 23 starts with section 22 (d), which provides that "distributions by corporations shall be taxable to shareholders as provided in section 115." Referring next to subsection (c) of section 115, they point out that although "amounts distributed in complete liquida-

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[2]Sec. 22. (d) Distributions by Corporations.—Distributions by corporations shall be taxable to the shareholders as provided in section 115.

Sec. 115. (c) Distributions in Liquidation.—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. In the case of amounts distributed in partial liquidation (other than a distribution within the provisions of section 112(h) of stock or securities in connection with a reorganization) the part of such distribution which is properly chargeable to capital accounts shall not be considered a distribution of earnings or profits within the meaning of subsection (b) of this section for the

tion of a corporation shall be treated as in full payment in exchange for the stock" the "gain or loss to a distributee resulting from such exchange" is determined under section 111, and "recognized" to the extent provided in section 112. Our attention is then called to the fact that by the terms of section 112 (a), the entire amount of gain or loss "upon the sale or exchange" of property "shall be recognized" except as thereafter provided in that section. It is then concluded that since the remaining provisions of section 112 contain no limitation or prohibition of the recognition of a loss resulting from complete liquidation of a corporation, the entire amount of the loss is recognized, and being recognized in full, its deduction is in no way de-

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purpose of determining the taxability of subsequent distributions by the corporation.

Sec. 111. (a) Computation of Gain or Loss.—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113(b), and the loss shall be the excess of such basis over the amount realized.

* * * * * * *

(c) Recognition of Gain or Loss.—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

Sec. 112. (a) General Rule.—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

pendent upon or limited by the provisions of section 23. [20]

The fallacies in this argument are elementary and obvious, and are at once apparent upon examination of the structure and plan of the income tax statute. The tax is imposed on net income and, according to section 21, net income is "gross income computed under section 22, less the deductions allowed by section 23." Section 22 provides generally that gross income "includes gains, profits, and income * * * of whatever kind and in whatever form paid, or from * * * any source whatever." It also enumerates certain specific items that are to be included in gross income and others that are to be excluded. Section 23 enumerates and describes the allowable deductions referred to in section 21. It is argued in this connection that sections 112 to 120, inclusive, are relief or distinctive provisions, and to rule that their application is to be made with reference to section 23 would amount to their repeal or nullification. We find nothing in any of these sections to indicate that the so-called or distinctive provisions are to be applied without reference to section 22 if they involve items of gain or profit, or without reference to section 23 if they involve losses or other charges allowable against gross income. On the other hand, Congress has particularly and specifically brought the application of these so-called relief sections within the provisions of sections 22 and 23. Illustrations are numerous. Subsection (b) (7) of section 22 provides for the exclusion from

gross income of the items of gain set forth in section 116, while subsections (g), (h), (i), (l), (m), and (n) of section 23 specifically give effect to the provisions of sections 113, 118, 117, 114 (b), (3), and (4), 114, and 120, respectively. It is thus apparent from the general plan of the statute that, in the absence of specific language to the contrary, deductions from gross income are allowable by and through the provisions of section 23 only. No other method of determining net income is provided.

The petitioners seek to vary the general plan of the statute by arguing that losses resulting to stockholders from corporate liquidations are to be given effect through section 22 (d). That argument is, in short, a claim that a loss deduction may be taken in the form of a minus or negative item of gross income, under the gross income provisions of the statute and without regard to the provisions of section 23. Obviously the provision in section 22 (d), to the effect that "distributions by corporations shall be taxable to shareholders as provided in section 115", is not susceptible of such strained construction.

The argument made here would also permit the deduction of a loss from the sale of stocks or securities on the market, without regard to section 23, since section 112 (a) provides that such a loss is to be recognized in full, there being no subsequent provision in that section [21] providing otherwise. Such reasoning would completely nullify the provisions of section 23 (e), (f), and (r) (1). The recognition

or nonrecognition of gain or loss under section 112 is in no sense a determination that the gain is to be included in gross income or that the loss is to be deducted therefrom. It is merely a determination as to whether or not the gain or loss is to be given such tax significance as the statute provides in the year in which the transaction giving rise to the gain or loss occurred, or is to be postponed until the happening of a further transaction in a subsequent year. Even though recognized, the tax effect of the gain or loss in computing net income is to be determined through the application of the gross income and deduction provisions of the statute. The result here being a recognized loss, the extent to which that loss is deductible is determined by the provisions of section 23.

In their reply brief the petitioners make the further contention that the limitation prescribed by section 23 (r) (1), on loss deductions, is not applicable here on the ground that a loss sustained in the disposition of stock in a corporate liquidation is not a loss from the sale or exchange of stock within the meaning of the statute. The reasoning advanced is that Congress, through sections 22 (d) and 115 (c), on the one hand, and sections 22 (e) and 111 (a) and (b) on the other, has carefully drawn a distinction between the disposition of stock in liquidation and an ordinary sale or exchange of stock on the market, and that the disallowance or limitation under section 23 (r) (1), of a loss sustained in the disposition of stock in liquidation requires the dis-

tortion or disregard of other pertinent provisions of the statute. It is also claimed that section 23 (r) (1) is applicable only to losses sustained in a sale or exchange of stocks and bonds on the market, because the Congressional Committees, in stating reasons for the insertion of section 23 (r) (1) in the statute, made specific reference to sales or exchanges on the market and no reference to the disposition of stock in a corporate liquidation.

It is well established that the reports of Congressional Committees may be resorted to as an aid to construction when the terms of the statute are contradictory or ambiguous, or the meaning of the words used is doubtful. Caminetti v. United States, 242 U. S. 470; Penn Mutual Life Insurance Co. v. Lederer, 252 U. S. 523. But it is equally well established that the intent of the lawmaker must be sought in the language of the statute, and where that language is clear and unambiguous, it must be enforced according to its terms and may not be varied or limited by reference to committee reports. The plain language of the statute may not be cast aside for other language thought by some one to have been in the mind of the legislative body. Congress must be presumed to have meant what it has said. Crooks v. [22] Harrelson, 282 U. S. 55; United States v. Goldenberg, 168 U. S. 95; Helvering v. City Bank Farmers Trust Co., 296 U. S. 85; Edith M. O'Donnell, 35 B. T. A. No. 37. From a consideration of the cases before us and the provisions of the statute involved, it does not appear here that

the aid of the Committee reports is invoked because the language of section 23 (r) (1) is ambiguous, but because the petitioners desire to limit and restrict the application of that language to the situations covered by specific illustrations in those reports. Clearly the cases cited do not permit reference to legislative history for such purposes, and where there is no ambiguity the language of the statute is controlling.

In support of their claim for a narrow and restricted application of section 23 (r) (1), the petitioners have cited numerous court decisions which deal with the interpretation and construction of statutes. It is our opinion that the cases cited generally support the respondent rather than the petitioners. In Helvering v. Stockholm Enskilda Bank, 293 U. S. 84, the Supreme Court stated that the intention of Congress, with reference to a particular provision of a taxing statute, is to be determined not by viewing the provision apart and separate from its setting in the act, but by considering it in connection with the context, general purpose of the statute in which it is found, and the occasion and circumstances of its use. In section 115 (c), on which petitioners base their claim for distinction, it is provided that amounts distributed in complete liquidation of a corporation are to be treated "as in full payment in exchange for the stock." It is then provided that the amount of gain or loss is to be "determined under section 111" and recognized "to the extent provided in section 112." These sec-

tions deal generally with the "sale or exchange" or "the sale or other disposition" of property. It thus appears by direct reference to other sections of the statute, that the disposition of corporate stock in liquidation is to be treated, for income tax purposes, as a "sale or exchange" and the distinction claimed by the petitioners is refuted by the plain words of the statute. Furthermore, it is interesting to note that if any doubt did exist and there were any basis for a claim of ambiguity, the report of the Committee on Ways and Means of the House of Representatives submitted with the bill which became the Revenue Act of 1924, in which report the language used in section 115 (c) was inserted, definitely indicates that the disposition of stock in a corporate liquidation is, for income tax purposes, a sale. The Committee there said: "The proposed bill, as did the 1918 Act, treats a liquidating dividend as a sale of the stock to the corporation and recognizes the true effect of such a distribution." [23]

The deduction of recognized losses in the case of an individual is governed by the provisions of subsection (e) of section 23, and, if a corporation, by the provisions of subsection (f). In both of these subsections it is provided that the deductions so allowed are subject to the limitation provided in subsection (r), paragraph (1) of which has been quoted above. The language of that limitation is plain and the deduction of any loss resulting from the sale or exchange of stocks or bonds, not capital assets, is limited in amount to gains derived from the sale or exchange of similar assets. In the cases

before us the preferred stock of the Townsend Co. was disposed of in liquidation of that company. The stock did not constitute capital assets in the hands of the petitioners and they make no claim that they realized any gains from the sale of similar assets. This disposition of the stock, under the provisions of the statute considered above, was a sale or exchange and the deduction of the losses sustained is barred by the provisions of section 23 (r) (1) of the statute.

Reviewed by the Board.

Decision will be entered under Rule 50.

Smith, dissenting: It is a cardinal principle of statutory construction that taxing statutes should be interpreted according to the intent of the legislative body enacting them. Thus, in Smythe v. Fiske, 23 Wall. 374, the Supreme Court said:

> A thing may be within the letter of a statute and not within its meaning, and within its meaning, though not within its letter. People v. The Utica Insurance Co., 15 Johnson, 380; Atkins v. The Fibre Disintegrating Co., 18 Wallace, 301; Bacon's Abridgment, title Statutes, 1, 2, 3, 5. The intention of the lawmaker is the law.

In Helvering v. New York Trust Co., 292 U. S. 455, the Supreme Court said:

> The rule that, where the statute contains no ambiguity, it must be taken literally and given

effect according to its language, is a sound one not to be put aside to avoid hardships that may sometimes result from giving effect to the legislative purpose. Commr. of Immigration v. Gottlieb, 265 U. S. 310, 313, 44 S. Ct. 528, 68 L. Ed. 1031; Bate Refrigerating Co. v. Sulzberger, 157 U. S. 1, 37, 15 S. Ct. 508, 39 L. Ed. 601. But the expounding of a statutory provision strictly according to the letter without regard to other parts of the act and legislative history would often defeat the object intended to be accomplished. Speaking through Chief Justice Taney in Brown v. Duchesne, 19 How. 183, page 194, 15 L. Ed. 595, this court said: "It is well settled that, in interpreting a statute, the court will not look merely to a particular clause in which general words may be used, but will take in connection with it the whole statute (or statutes on the same subject) and the objects and policy of the law, as indicated by its various provisions, and give to it such a construction as will carry [24] into execution the will of the Legislature, as thus ascertained, according to its true intent and meaning." Quite recently in Ozawa v. United States, 260 U. S. 178, page 194, we said: "It is the duty of this Court to give effect to the intent of Congress. Primarily this intent is ascertained by giving the words their natural significance, but if this leads to an unreasonable result plainly at variance with the policy of the legislation as

a whole, we must examine the matter further. We may then look to the reason of the enactment and inquire into its antecedent history and give it effect in accordance with its design and purpose, sacrificing, if necessary, the literal meaning in order that the purpose may not fail."

And in Barrett v. Van Pelt, 268 U. S. 85, 90, 45 S. Ct. 437, 439, 69 L. Ed. 857, we applied the rule laid down in People v. Utica Ins. Co., 15 Johns. (N. Y.) 358, 381, 8 Am. Dec. 243, that "a thing which is within the intention of the makers of a statute is as much within the statute as if it were within the letter, and a thing which is within the letter of a statute, is not within the statute, unless it is within the intention of the makers."

Did the Congress by section 23 (r) intend to prevent corporate stockholders sustaining losses upon the liquidation of corporations from deducting those losses from gross income except to the extent of gains realized from sales or exchanges of stocks and bonds? I think not.

The legislative history of section 23 (r) of the Revenue Act of 1932 shows that that provision was designed to prevent corporate stockholders from deducting from gross income losses created through sales or exchanges "in the stock and bond markets." The Ways and Means Committee Report 708 on H. R. 10236, which later became the Revenue Act of 1932, comments upon five proposed additions to

section 23 of the Revenue Act of 1928, i.e., subsections (r), (s), (t), (u), and (v). These proposed subsections emerged in amended form as subsections (r), (s), and (t) of the Revenue Act of 1932. In presenting the five proposed additions to the House Bill, the Ways and Means Committee Report stated, p. 12:

> Many taxpayers have been completely eliminating from tax their income from salaries, dividends, rents, etc., by deducting therefrom losses sustained in the stock and bond markets, with serious effect upon the revenue. Your committee is of the opinion that some limitation ought to be placed on the allowance of such losses.

After referring to the exclusion of "dealers in securities", as provided in subsection 23 (r) (3), the Committee reports stated:

> Traders or other taxpayers who buy and sell securities for investment or speculation, whether or not in their own account, and irrespective of whether such buying or selling constitutes the carrying on of a trade or business, are not regarded as dealers in securities within the meaning of this rule.

The Finance Committee Report of the Senate on this same bill (Report 665, p. 12) contains the following: [25]

> The House Bill adopted very severe limitations upon the allowance of losses from the sale

> of securities, as a deduction in computing net income. The provision is based upon a twofold policy: (1) Protecting the revenues from the growing practice of reducing tax liabilities by the sale of securities on which losses had accrued, and (2) preventing speculative losses from wiping out ordinary income, which represents real tax-paying ability.

There is nothing in the Committee reports which tends in the slightest to show that section 23 (r) had in contemplation losses sustained through the liquidation of corporations.

Section 22 (d) of the Revenue Act of 1928 provides that "Distributions by corporations shall be taxable to the shareholders as provided in section 115", and section 115 (c) provides in part:

> Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. * * *

The Revenue Act of 1928 contained no provision corresponding to section 23 (r) of the Revenue Act of 1932. Section 22 (d) and section 115 (c) of the Revenue Act of 1928 were incorporated and made a part, without change, of the Revenue Act of 1932.

Where corporations are liquidated, stockholders receiving liquidation distributions may or may not turn in their shares of stock. It is a common thing

for them to do so. See Phelps v. Commissioner, 54 Fed. (2d) 289. Whether they do so or not, however, they are treated as exchanges under both the Revenue Act of 1928 and that of 1932 for the purpose of giving corporate stockholders the benefits of sections 111 and 112.

The word "exchange" in its ordinary meaning carries with it the idea of mutual agreement--a transfer of property for property in a transaction freely arrived at between two parties. See Law v. McLaughlin, 2 F. Supp. 601. These elements are lacking where in distributions in liquidation a stockholder has no alternative but to surrender his shares of stock and receive his proportion of the assets of the corporation distributable to him. Section 115 (c) does not provide that distributions in liquidation shall constitute "exchanges." It simply provides that they shall be treated as in full or part payment "in exchange" for the stock.

In section 23 (r) of the Revenue Act of 1932 the word "exchange" is coupled with the word "sales." Under the doctrine of ejusdem generis the word "exchanges" must be interpreted in the light of the word with which it is associated. Losses sustained upon sales of stocks and bonds are subject to the limitation of section 23 (r) (1). If the word "exchanges" had not been used in this provision the very evil at which section 23 (r) was aimed might have been perpetuated [26] by corporate stockholders exchanging their stocks and bonds for other securities or other property. Such circumvention of

the statute was forestalled by the language used by the draftsmen of the act.

In the light of the legislative history of section 23 (r) I can not believe that Congress had any intention of limiting the deduction from gross income of losses sustained by taxpayers in the liquidation of corporations.

Black, Tyson, Hill, and Harron agree with this dissent. [27]

United States Board of Tax Appeals
Docket No. 82865, 82870, 82871.

CHESTER N. WEAVER COMPANY,
CHESTER N. WEAVER,
ELSIE S. WEAVER,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the Findings of Fact and Opinion of the Board promulgated February 17, 1937, the respondent herein, on February 27, 1937 filed a notice of settlement and proposed recomputation, and the petitioner herein, having on March 12, 1937 filed an acquiescence in the recomputation as made by the respondent, it is

ORDERED and DECIDED, that there are deficiencies in income tax for the year 1933 as follows:

Name	Docket No.	Amount:
Chester N. Weaver Company,	82865	$4,323.48
Chester N. Weaver,	82870	8,832.43
Elsie S. Weaver,	82871	2,447.84

Enter:

[Seal] BOLON B. TURNER,
Member.

Entered Mar 20 1937. [28]

[Title of Court and Cause.]

PETITION OF CHESTER N. WEAVER COMPANY, A CORPORATION, FOR REVIEW BY THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT OF A DECISION BY THE UNITED STATES BOARD OF TAX APPEALS IN THE ABOVE ENTITLED PROCEEDING.

Chester N. Weaver Company, a corporation, the petitioner in the above entitled proceeding hereby files this petition for a review by the United States Circuit Court of Appeals for the Ninth Circuit of a decision of the United States Board of Tax Appeals rendered against it (promulgated February 17, 1937, 35 B. T. A. No. 76 and entered March 20, 1937,) determining a deficiency in petitioner's Federal income tax for the calendar year

1933 in the amount of $4,323.48, and in and by this petition respectfully shows:

I.

JURISDICTION

Petitioner Chester N. Weaver Company is and at all the times herein mentioned was a corporation duly organized [29] and existing under the laws of the State of California, with its principal place of business in the City and County of San Francisco in said State. Petitioner filed its Federal income tax return for the calendar taxable year 1933 with the United States Collector of Internal Revenue for the First District of California in the office of said Collector located in said City and County of San Francisco and within the jurisdiction of the United States Circuit Court of Appeals for the Ninth Circuit.

II.

PRIOR PROCEEDINGS

Respondent, on December 30, 1935, claimed and determined additional income tax for the taxable calendar year 1933 against petitioner in the amount of $4,323.48, and as required by section 272 of the Revenue Act of 1932 respondent on said day sent to petitioner by registered mail a notice of such deficiency. On February 4, 1936, petitioner appealed to the United States Board of Tax Appeals from such proposed determination of deficiency and on March 24, 1936, respondent filed his answer to such appeal.

Thereafter, and on July 6, 1936, the appeal of petitioner was consolidated for hearing and decision with the appeals of Chester N. Weaver, Docket No. 82870, and Elsie S. Weaver, Docket No. 82871, by order of the United States Board of Tax Appeals and the three appeals were then submitted for decision on a stipulation of facts applicable to the one and only question at issue in said three appeals.

Thereafter and on February 17, 1937, said Board of Tax Appeals promulgated its finding of fact and opinion in the consolidated proceedings and on March 20, 1937, entered its [30] final order and decision therein and ordered and decided that there was a deficiency in petitioner's Federal income tax for the year 1933 in the amount of $4,323.48.

III.

NATURE OF CONTROVERSY

The controversy involves the proper determination of petitioner's Federal income tax for the calendar year 1933. The question is whether petitioner sustained a deductible loss in the amount of $86,859.75 in a transaction entered into for profit.

During the year 1931 and years prior thereto Chester N. Weaver Company (hereinafter referred to as Weaver Company) was engaged in the business of distributing and selling Studebaker and Pierce-Arrow automobiles in the City and County of San Francisco and the cities of Oakland and Berkeley, Alameda County, State of California.

In November of 1931 Weaver Company decided to dispose of its business of distributing and selling automobiles. One Jeff R. Townsend organized a corporation under the name of "Jeff R. Townsend Company, Inc." (hereinafter referred to as Townsend Company) on November 25, 1931, for the purpose of purchasing the automobile business of Weaver Company. The new corporation had an authorized capital stock of 5,000 shares of a par value of $100. per share, of which 3,000 shares were common and 2,000 shares were preferred. Jeff R. Townsend and Earl R. Carpenter subscribed and paid for 500 shares of said common stock at par. On August 9, 1932, petitioner purchased from said Townsend Company 1000 shares of its preferred stock [31] and paid $100,000 therefor. From said last mentioned date to September 18, 1933, when said Townsend Company was liquidated, a period of less than two years, petitioner was at all times the owner and holder of said 1,000 shares of said preferred stock.

During the early part of 1933, prior to March 28, 1933, the Townsend Company became financially involved and unable to continue its business. On March 28, 1933, at a meeting of its stockholders, it was determined to close the affairs of the Townsend Company and voluntarily liquidate and dissolve the corporation. Thereafter and during the month of September, 1933, said corporation was finally liquidated and dissolved by voluntary proceedings.

In the liquidation of said Townsend Company and after payment of its liabilities but $26,280.50 of its capital remained for distribution to its stockholders. As this amount was inadequate to satisfy the preference of the preferred stockholders, said $26,280.50 was distributed pro rata to the preferred stockholders in complete liquidation of said corporation and none of the assets of such corporation were distributed to the common stockholders. On said distribution in final liquidation of said Townsend Company petitioner received only the amount of $13,140.25.

Petitioner kept its accounts and made its income tax return for the calendar year 1933 on a cash receipts and disbursements basis and deducted the difference between the amount of $100,000 paid for said 1000 shares of said preferred stock and said amount of $13,140.25 received for said shares in liquidation, or $86,859.75, as a loss sustained in the taxable year 1933. Respondent disallowed said deduction. [32]

Petitioner contended before the United States Board of Tax Appeals that it was entitled to deduct the loss of $86,859.75 asserted and deducted by it in its income tax return for 1933 under the provisions of sections 22(d), 115(c), 111 and 112(a) of the Revenue Act of 1932.

Said Board of Tax Appeals held that section 23(r) (1) of said revenue act barred the deduction sought.

Petitioner, being aggrieved by the findings of fact and conclusions of law contained in the findings and

opinion of said Board of Tax Appeals and by its decision entered pursuant thereto, desires to obtain a review thereof by the United States Circuit Court of Appeals for the Ninth Circuit.

IV.

ASSIGNMENTS OF ERROR

Petitioner assigns as error the following acts and omissions of the United States Board of Tax Appeals:

(1) The failure to allow the amount of $86,859.75 as a deductible loss sustained by petitioner during the taxable year 1933 and as a deduction from petitioner's gross income for said year within the intendment of section 23 of the Revenue Act of 1932.

(2) The failure to give proper effect to the provisions of sections 22(d), 115(c), 111 and 112(a) of the Revenue Act of 1932 in determining petitioners net taxable income for the calendar year 1933.

(3) The failure to interpret section 23(r) (1) of the Revenue Act of 1932 in accordance with the purpose and intent of that section and the meaning of Congress in enacting that section. [33]

(4) The failure to find that petitioner sustained a deductible loss in the amount claimed for the year 1933.

(5) The holding that petitioner is liable for a deficiency for the year 1933 in lieu of a determination that there is no income tax due from petitioner for the year in controversy.

Wherefore, petitioner prays that the decision of the United States Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Ninth Circuit; that a transcript of the record be prepared in accordance with law, the rules of said Court and the rules and practice of said Board of Tax Appeals for filing, and that appropriate action be taken to the end that the errors complained of herein be reviewed and corrected by said Court.

ADOLPHUS E. GRAUPNER
ARTHUR E. COOLEY
Counsel for Petitioner,
1110 Balfour Building,
San Francisco, California

[34]

State of California
City and County of San Francisco—ss.

Chester N. Weaver, being first duly sworn deposes and says that he is the President of the Chester N. Weaver Company, a corporation and the petitioner herein, and as such is authorized to verify the foregoing petition; that he has read the foregoing petition and knows the contents thereof; that to the best of his knowledge and belief the statements therein are true and the assignments of error are well taken and intended to be argued.

CHESTER N. WEAVER

Subscribed and sworn to before me this 12th day of April, 1937.

[Seal] EMILY K. McCORRY

Notary Public in and for the City and County of San Francisco, State of California.

My Commission expires January 16, 1939.

[Endorsed]: U.S.B.T.A. Filed Apr. 20, 1937. [35]

[Title of Court and Cause—Docket Nos. 82865, 82870, 82871.]

STIPULATION OF FACTS.

It is hereby stipulated and agreed by and between parties hereto, by their respective attorneys of record, that the following facts shall be taken as true; provided, however, that this stipulation shall be without [36] prejudice to the right of either party to introduce other and further evidence not inconsistent with the facts herein stipulated to be true; and provided, further, that when offered in evidence this stipulation shall be subject to objection by either party hereto as to relevancy or materiality of all or any part hereof.

It is further stipulated and agreed that, subject to the conditions of the preceding paragraph, and insofar as the facts stated are relevant and material respectively to the above entitled proceedings, the following facts shall be considered as evidence in the said proceedings, Docket Nos. 82865, 82870, 82871:

1. Chester N. Weaver Company (hereinafter referred to as Weaver Company), petitioner in proceeding numbered 82865, is and at all the times hereinafter mentioned was a corporation duly organized and existing under the laws of the State of California.

2. Chester N. Weaver, petitioner in proceeding numbered 82870, is and at all the times hereinafter mentioned was an individual domiciled in the City and County of San Francisco, State of California.

3. Elsie S. Weaver, petitioner in proceeding numbered 82871, is and at all the times hereinafter mentioned was an individual domiciled in the City and County of San Francisco, State of California.

4. Said Chester N. Weaver and Elsie S. Weaver [37] are and at all the times hereinafter mentioned were husband and wife, living together as such and residing in the said City and County of San Francisco.

5. Jeff R. Townsend Company, Inc. (hereinafter referred to as Townsend Company) was incorporated under the laws of the State of California on November 25, 1931, with an authorized capital stock of five thousand shares of a par value of $100. per share, of which authorized shares, three thousand were shares of common stock and two thousand were shares of preferred stock. During the month of September, 1933, the said Townsend Company was liquidated, its assets were distributed and it was formally dissolved as a corporation by voluntary proceedings.

6. The articles of incorporation of the said Townsend Company provided for the two classes of shares of its capital stock, as follows:

Fifth: That the following is a statement of the preferences, privileges and restrictions granted to or imposed upon the holders of the respective classes of shares:

(a) All rights to vote and all voting power are hereby vested exclusively in the holders of the common stock, provided, however, that if there shall be a default or omission in the payment of four quarterly dividend payments on said preferred stock, then the preferred stockholders shall be given notice of all stockholders meetings to be held thereafter and shall have the same rights as the common stockholders to vote at said meetings, but such right to vote shall continue only during such period as the corporation [38] shall be in default in the payment of said dividends. This right to vote shall not deprive the preferred stockholders of the exercise of any right which they may have at law or in equity to enforce any of the provisions with respect to preferred stock.

(b) When fully paid, the preferred stock of this corporation shall be nonassessable.

(c) The holders of the preferred stock of this corporation shall be entitled to receive dividends thereon from the surplus profits of the corporation arising from its business, to the extent that the corporation may lawfully pay

the same, at the rate of six per cent of the par value thereof, per annum, and no more, from the date when issued, payable in equal quarterly installments on the first days of January, April, July and October of each calendar year, provided, however, that the first dividend thereon shall be paid on April 1st, 1932, which first dividend shall be at said rate of six per cent per annum from the date of issuance of the preferred stock then outstanding. Such dividends shall be cumulative and shall be paid in full, for each such dividend period, and for all cumulations of unpaid dividends, before any dividends upon the common stock shall be paid or set apart for payment.

(d) Whenever all dividends accrued upon the preferred shares shall have been paid, or payment thereof tendered, the board of directors of this corporation may declare and pay to the holders of the outstanding common shares dividends thereon from the remaining undistributed profits of the corporation, but said dividends upon common shares shall not be cumulative.

(e) In the event of the dissolution of this corporation or the winding up of its affairs or of the distribution of its assets for any other reason, the holders of such preferred stock shall be entitled to receive, for each share thereof, out of the assets of the corporation, and before any of said assets shall be distributed to the holders of common stock, a sum equal to one hundred five per cent. of the par

value thereof, plus an amount equal to all unpaid dividends then accrued thereon, provided that if said distribution shall be made more than five years after the date of incorporation of this corporation, then the holders of such preferred stock shall be entitled to receive a sum equal to the par value thereof, plus said unpaid dividends then accrued; and, after said payments to said holders of preferred stock shall have been made [39] all of the residue of such assets shall be paid and distributed ratably to and among the holders of the common stock.

(f) The corporation may, at its option, redeem any number of such preferred shares upon any dividend paying date by paying to the holder thereof, for each share redeemed, a sum equal to one hundred five per cent. of the par value thereof, plus an amount equal to all unpaid dividends then accrued thereon, provided that if said redemption shall be made more than five years after the date of incorporation of this corporation, then such shareholder shall be paid a sum equal to the par value of such shares, plus said unpaid dividends then accrued. As a condition precedent to the right of the corporation to redeem said preferred stock, it shall give the shareholder, whose shares it proposes to redeem, written notice of its intention so to redeem at least thirty days prior to

the dividend date upon which redemption is to be made. Said preferred shares so redeemed shall not be reissued.

7. During the year 1931 said Weaver Company was engaged in the business of selling automobiles in the City and County of San Francisco and in the Cities of Oakland and Berkeley, Alameda County, as distributor and agent of Studebaker and Pierce-Arrow automobiles. During the month of November, 1931, the Weaver Company determined to dispose of its agency and business. The above-described Townsend Company was organized by Jeff R. Townsend, San Diego distributor of and agent for Studebaker automobiles, for the purpose of purchasing the San Francisco agency and business of the Weaver Company. On or about December 17, 1931, said Townsend Company purchased all of the physical assets of the Weaver Company, excepting real property, which were located in San Francisco, including its entire stock of automobiles, furniture [40] and fixtures, machinery and tools, and equipment located in the Weaver Building, Bush Street and Van Ness Avenue, San Francisco. On or about July 26, 1932, said Townsend Company purchased all of the physical assets of the Weaver Company excepting real property, which were located in Alameda County, in the cities of Oakland and Berkeley including its entire stock of automobiles, furniture and fixtures, machinery and tools, and equipment.

8. At the time of organization of said Townsend Company, Jeff R. Townsend and Earl R. Carpenter subscribed and paid for five hundred shares of the common stock of said company at par and each of said Chester N. Weaver and said Elsie S. Weaver subscribed for five hundred shares of the preferred stock of said company. On December 2, 1931, Chester N. Weaver paid $50,000. and Elsie S. Weaver paid $50,000. to said Townsend Company for said shares of stock and certificates for five hundred shares of preferred stock were thereupon delivered to each of said Chester N. Weaver and Elsie S. Weaver.

9. Thereafter and until the certificates for said shares of preferred stock were surrendered for cancellation on liquidation of the said Townsend Company on September 18, 1933, each of said Chester N. Weaver and said Elsie S. Weaver continued to be the owner and holder of five hundred shares of preferred stock of said Townsend Company.

10. On August 9, 1932, said Weaver Company purchased from said Townsend Company one thousand shares of [41] its preferred stock and paid to said Townsend Company for said shares the sum of $100,000. Thereafter and until the certificate for said shares of preferred stock were surrendered for cancellation on liquidation of the said Townsend Company on September 18, 1933, said Weaver Company continued to be the owner and holder of one thousand shares of the preferred stock of said Townsend Company.

11. Dividends at the rate of six per centum per annum were declared by the Townsend Company upon its issued preferred capital stock on April 2, 1932, July 2, 1932, and October 3, 1932.

12. During the early part of 1933 and prior to March 28, 1933, said Townsend Company became financially involved and unable to continue its business and on March 28, 1933, a meeting of the stockholders was held for the purpose of considering the question of closing up the affairs of the company and voluntarily dissolving the corporation. At such meeting a resolution was adopted by vote of the holders and owners of all the common stock of the corporation authorizing the liquidation and dissolution of the company and directing the President and Secretary to execute the corporate certificate giving notice of intention to dissolve as required by law. At said meeting, by resolution adopted by vote of the holders and owners of all the common stock of the corporation, Chester N. Weaver was appointed agent of said Townsend Company for the purpose of supervising [42] the closing of its business affairs to effect its dissolution.

13. On March 28, 1933, following the above-mentioned stockholder's meeting, a meeting of the directors of the said Townsend Company was held. At such meeting the directors of the corporation appointed Chester N. Weaver as agent to close the business affairs of the company and take all necessary steps to effect its dissolution.

14. Thereafter proceedings were taken for the liquidation of the business affairs of the Town-

send Company and on September 16, 1933, the directors, at a special meeting called for that purpose, adopted a resolution authorizing the corporation to sell "all of its remaining assets, tangible and intangible to the Chester N. Weaver Co. for the sum of $26,280.50 and the assumption by Chester N. Weaver Co. of all the outstanding debts and liabilities of Jeff R. Townsend Company, Inc." Thereafter and about September 17, 1933, said Townsend Company transferred and delivered all of its remaining assets to said Weaver Company and said Weaver Company paid the amount of $26,280.50 therefor to said Townsend Company.

15. On September 18, 1933, all of the stockholders of the Townsend Company surrendered their certificates for shares of stock in the corporation for cancellation for the purpose of completing liquidation and effecting dissolution of said company. The said Weaver Company surrendered for cancellation two preferred stock certificates, each for [43] five hundred shares; said Chester N. Weaver surrendered for cancellation one preferred stock certificate for five hundred shares, and said Elsie S. Weaver surrendered for cancellation one preferred stock certificate for five hundred shares. Jeff R. Townsend surrendered for cancellation one common stock certificate for two hundred shares and Earl R. Carpenter surrendered for cancellation one common stock certificate for three hundred shares. The certificates thus surrendered represented all of the capital stock of said Townsend Company.

16. On surrender of the preferred stock certificates as above described, the entire assets of said Townsend Company, consisting of $26,280.50, were distributed to the owners and holders of such preferred stock, as follows: to said Weaver Company, $13,140.25; to Chester N. Weaver, $6,570.13; and to Elsie S. Weaver, $6,570.12. The assets of the said corporation being insufficient to pay the holders of the preferred stock "a sum equal to one hundred and five per cent of the par value thereof", or the par value thereof, no part of the said assets was distributed to the common stockholders.

17. Each of the four certificates for preferred stock surrendered as above described was endorsed on the back thereof as follows:

"San Francisco, California,
September 18, 1933

"This certificate surrendered to Jeff Townsend Co. Inc. upon payment of $ as final [44] payment on this stock as per distribution of assets."

The amount of $6,570.12 was written after the symbol $ in the endorsement on Chester N. Weaver's certificate, $6,570.13 in Elsie S. Weaver's certificate and $6,570.12 on one certificate of Chester N. Weaver Co. and $6,570.13 on the other certificate of Chester N. Weaver Co. Each of said endorsements was signed by the owner and holder of the certificate surrendered. The two certificates for common stock of said Townsend Company, surrendered respectively by Jeff R. Townsend and Earl R. Carpenter, bore no endorsement other than the

usual blank form of endorsement for transfer signed by the respective stockholders:

18. None of the petitioners in the above named proceedings received any other assets or amount than that as set forth hereinabove in paragraph numbered 16 from the liquidation, distribution of assets and dissolution of said Townsend Company.

19. In its income tax return for the taxable year 1933, said Weaver Company deducted from its returned income the amount of $86,859.75 as a loss resulting from the liquidation of said Townsend Company.

In his income tax return for the taxable year 1933, said Chester N. Weaver deducted from his returned income the amount of $43,429.87 as a loss resulting from the liquidation of said Townsend Company.

In her income tax return for the taxable year [45] 1933, said Elsie S. Weaver deducted from her returned income the amount of $43,429.87 as a loss resulting from the liquidation of said Townsend Company.

Respondent disallowed the deductions taken by the respective petitioners as above set forth and thereupon determined the deficiencies at issue in the above entitled proceedings.

20. The respondent disallowed the losses deducted by the respective petitioners in the above entitled proceedings as set forth in the preceding paragraph and the sole issue for determination by the United States Board of Tax Appeals in each

of the above entitled proceedings is whether said deductions are properly allowable under the Revenue Act of 1932.

21. The copies of the deficiency notice attached to each of the petitions in the above entitled proceedings are stipulated to be true copies of such notices and are admitted as evidence on behalf of the respective petitioners as Exhibit No. 1 in each of the above entitled proceedings.

22. Photostatic copies of the income tax [46] returns of the respective petitioners filed herewith by respondent are stipulated to be true copies and are respectively admitted as evidence on behalf of respondent as Exhibit A in each of the above entitled proceedings.

ADOLPHUS E. GRAUPNER
ARTHUR E. COOLEY
Attorneys for Petitioners
Chester N. Weaver Company
Chester N. Weaver
Elsie S. Weaver.

HERMAN OLIPHANT O. W. S.
General Counsel for the Department of the Treasury
Attorney for Respondents.

[Endorsed]: U. S. B. T. A. Filed at hearing July 6, 1936. [47]

[Title of Court and Cause Docket Nos. 82865, 82,-870, 82871.]

STIPULATION AND ORDER FOR CONSOLIDATION ON REVIEW

Whereas, the above entitled three proceedings involve similar facts and presented the same question and issue for decision by the United States Board of Tax Appeals; and [48]

Whereas, under order of said Board the above entitled proceedings were consolidated for hearing and decision and but one findings of fact, opinion and decision was made by said Board in and for said three proceedings; and

Whereas, separate petitions for review of said consolidated findings, opinion and decision by the United States Circuit Court of Appeals for the Ninth Circuit, with separate assignments of errors have been filed with said Board on behalf of each of the above named petitioners in the proceedings respectively instituted by them; and

Whereas, each of said petitions sets forth the same material facts and assignments of errors as the others, and the three petitions differ only in the titles of the petitioners and the amounts claimed as deductible losses therein; and

Whereas, the preparation and printing of the complete record in proceeding No. 82865, Chester N. Weaver Company v. Commissioner of Internal Revenue will be sufficient for the said Court to consider and dispose of the questions involved in the

three above entitled proceedings and will avoid the unnecessary expense of preparing and printing three separate records for review of the same questions of law;

Now, Threfore, It Is Hereby Stipulated and Agreed by and between all of the parties above named by their respective counsel as follows:

1. The Clerk of said United States Board of Tax Appeals shall prepare and transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, a complete record in proceedings No. 82865, Chester N. Weaver Company v. [49] Commissioner of Internal Revenue as follows:

(a) The docket entries of proceedings had before said Board in said proceedings No. 82865;

(b) The pleadings before said Board in said proceedings No. 82865 as follows:
(1) Petition for redetermination,
(2) Answer of the respondent;

(c) Minute order of said Board consolidating the three above entitled proceedings for hearing and decision;

(d) The findings of fact and opinion of said Board in proceedings No. 82865.

(e) The decision of said Board;

(f) The petition for review and assignment of errors filed by the petitioner Chester N. Weaver Company in proceedings No. 82865;

(g) The consolidated stipulation of facts filed with said Board in the above entitled pro-

ceedings, Docket Nos. 82865, 82870 and 82871;

(h) This stipulation and order;

(i) The praecipe for transcript of the record.

2. The Clerk of said United States Board of Tax Appeals shall prepare and transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit a skeleton record in each of the proceedings of Chester N. Weaver v. Commissioner of Internal Revenue, Docket No. 82870, and Elsie S. Weaver v. Commissioner of Internal Revenue, Docket No. 82871, as follows:

(a) Petition for review and assignment of errors filed by the respective petitioners in each of said two proceedings;

(b) Proof of service of said petitions for review and assignments [50] of errors in each proceeding;

(c) This stipulation and order; and

(d) The praecipe for transcript of the skeleton record in each proceeding;

3. That the Clerk of said United States Circuit Court of Appeals shall cause to be printed only the record in proceedings No. 82865, Chester N. Weaver Company v. Commissioner of Internal Revenue.

4. That no briefs need be filed by either party with the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit in the proceeding docketed as Nos. 82870 and 82871 in the said Board of Tax Appeals.

5. That the record on appeal from the decision of said Board of Tax Appeals in proceedings No. 82865, Chester N. Weaver Company v. Commissioner of Internal Revenue, contains all facts and records required by the above-mentioned Court to pass upon the questions of law involved in the three said proceedings docketed in said Board of Tax Appeals as Nos. 82865, 82870 and 82871.

6. That the decision of the United States Circuit Court of Appeals for the Ninth Circuit and any further proceedings of the said Board of Tax Appeals and the respondent herein shall be stayed in proceedings Nos. 82870 and 82871 until the decision in proceedings No. 82865 shall have become final in accordance with the provisions of Section 1005 of the Revenue Act of 1926.

7. That upon the final determination, decision and judgment on the appeal of Chester N. Weaver Company v. Commissioner of Internal Revenue (B. T. A. Docket No. 82865) either party to each of the proceedings of Chester N. Weaver v. Commissioner of Internal [51] Revenue (B. T. A. Docket No. 82870) and Elsie S. Weaver (B. T. A. Docket No. 82871) may apply, upon written notice to the other party, upon this stipulation, and upon a certified copy of the decision, order, or judgment of the United States Circuit Court of Appeals for the Ninth Circuit in the Appeal of Chester N. Weaver Company v. Commissioner of Internal Revenue for an order directing judgment to be entered in each of said proceedings (B. T. A.

Docket Nos. 82870 and 82871) in accordance with the final decision, order, or judgment in said appeal of Chester N. Weaver Company v. Commissioner of Internal Revenue.

Dated, May 17th, 1937.

(Signed) ADOLPHUS E. GRAUPNER
(Signed) ARTHUR E. COOLEY
MORRISON SHAFROTH
Chief Counsel
Bureau of Internal Revenue.
Counsel for Respondent. [52]

ORDER

Upon reading the foregoing stipulation and on motion on behalf of the parties thereto

It Is Hereby Ordered that the procedure stipulated by and between the parties to the above entitled proceeding shall be adopted and that the Clerk of this Court, the Clerk of the United States Board of Tax Appeals, Appellants and the Respondent shall act and proceed in accordance therewith.

Dated: May 17th, 1937.

CURTIS D. WILBUR
Senior Judge of the United States Circuit Court of Appeals for the Ninth Circuit.

[Endorsed]: U.S.B.T.A. Filed May 24, 1937. [53]

[Title of Court and Cause.]

PRAECIPE FOR RECORD

To the Clerk of the United States Board of Tax Appeals:

You are hereby requested to prepare and certify and transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, with reference to the petitioner for review heretofore filed by the petitioner in the above-entitled proceeding a transcript of the record in the above cause, prepared and transmitted as required by law and by the rules of said Court, and to include in said transcript of record the following documents or certified copies thereof, to-wit:

1. The docket entries of all proceedings had before the United States Board of Tax Appeals;

2. Pleadings before the said Board of Tax Appeals as follows:

(a) Petition for redetermination, and [54]

(b) Answer of the respondent;

3. Minute order of said Board consolidating the above entitled proceeding for hearing and decision with those of Chester N. Weaver, Docket No. 82870, and Elsie S. Weaver, Docket No. 82871;

4. The findings of fact and opinion of said Board;

5. The decision of said Board;

6. The petition for review and assignment of errors filed by the petitioner in the above-entitled proceeding:

7. The stipulation of facts filed with said Board in the above entitled proceeding and on which the cause was tried;

8. The stipulation and order for consolidation on review of the above-entitled proceeding with the said proceedings of Chester N. Weaver and Elsie S. Weaver dated May 17, 1937;

9. This Praecipe.

ADOLPHUS E. GRAUPNER
ARTHUR E. COOLEY
Attorneys for Petitioner

[Endorsed]: U.S.B.T.A. Filed May 24, 1937. [55]

[Title of Court and Cause.]

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 55, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 26th day of May, 1937.

[Seal] B. D. GAMBLE
Clerk, United States Board of Tax Appeals.

[Endorsed]: No. 8572. United States Circuit Court of Appeals for the Ninth Circuit. Chester N. Weaver Company, a corporation, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review a Decision of the United States Board of Tax Appeals.

Filed June 7, 1937.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

No. 8572

CHESTER N. WEAVER COMPANY, A CORPORATION, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Upon Petition to Review a Decision of the United States Board of Tax Appeals

Proceedings had in the United States Circuit Court of Appeals for the Ninth Circuit.

United States Circuit Court of Appeals for the Ninth Circuit

Excerpt from Proceedings of Wednesday, March 16, 1938

Before GARRECHT, HANEY, and STEPHENS, Circuit Judges

No. 8572

Order of submission

Ordered above cause argued by Mr. Adolphus E. Grauper, counsel for petitioner, and by Mr. M. Leo Looney, Special Assistant to the Attorney General, counsel for respondent, and submitted to the court for consideration and decision.

United States Circuit Court of Appeals for the Ninth Circuit

Excerpt from Proceedings of Thursday, June 2, 1938

Before GARRECHT, HANEY, and STEPHENS, Circuit Judges

No. 8572

Order directing filing of opinion and dissenting opinion, and filing and recording of judgment

By direction of the Court, ordered that the typewritten opinion and dissenting opinion this day rendered by this court in above cause be forthwith filed by the clerk, and that a judgment be filed and recorded in the minutes of this court in accordance with the majority opinion rendered.

United States Circuit Court of Appeals for the Ninth Circuit

No. 8572

CHESTER N. WEAVER COMPANY, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Upon Petition to Review a Decision of the United States Board of Tax Appeals.

This Cause came on to be heard on the Transcript of the Record from the United States Board of Tax Appeals and was duly submitted.

On Consideration Whereof, it is now here ordered and adjudged by this Court that the Decision of the said Board of Tax Appeals in this Cause be, and hereby is, reversed.

[Endorsed:] Judgment. Filed and entered June 2, 1938. Paul P. O'Brien, Clerk.

United States Circuit Court of Appeals for the Ninth Circuit

(Title of cause and number)

Certificate of Clerk, U. S. Circuit Court of Appeals for the Ninth Circuit, to record certified under rule 38 of the Revised Rules of the Supreme Court of the United States

I, Paul P. O'Brien, as Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, do hereby certify the foregoing eighty (80) pages, numbered from and including 1 to and including 80, to be a full, true, and correct copy of the entire record of the above-entitled case in the said Circuit Court of Appeals, made pursuant to request of Mr. N. A. Townsend, Acting Solicitor General of the United States, counsel for the respondent, and certified under Rule 38 of the Revised Rules of the Supreme Court of the United States, as the originals thereof remain on file and appear of record in my office.

Attest my hand and the seal of the said the United States Circuit Court of Appeals for the Ninth Circuit, at the City of San Francisco, in the State of California, this 1st day of August A. D. 1938.

[SEAL] (Sgd.) PAUL P. O'BRIEN, *Clerk.*

In the United States Circuit Court of Appeals for the Ninth Circuit

No. 8572. June 2, 1938

CHESTER N. WEAVER COMPANY, A CORPORATION, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Upon Petition to Review a Decision of the United States Board of Tax Appeals

Before GARRECHT, HANEY, and STEPHENS, Circuit Judges

HANEY, Circuit Judge.

Review is sought of a decision of the Board of Tax Appeals which sustained a determination of respondent that there was a deficiency in the income tax paid by petitioner for the year 1933.

Petitioner, a California corporation, on August 9, 1932, purchased from Jeff R. Townsend Company, Inc., a California corporation, hereinafter referred to as the Townsend company, 1,000 shares of the latter's preferred stock, paying therefor $100 per share. The Townsend company's articles of incorporation provided that in the event of liquidation, its preferred stockholders would be entitled to receive a sum equal to 105 per cent of the par value of the preferred stock before any amount would be distributed to the holders of its common stock.

In 1933, the Townsend company became financially involved and unable to continue its business. On September 17, 1933, in order to dissolve and liquidate, it sold all its assets for $26,280.50, which on the next day was distributed pro rata to its preferred stockholders, who at the same time surrendered their certificates for preferred stock. Petitioner received a liquidating dividend in the sum of $13,140.25.

In its income tax return for the year 1933, petitioner claimed a deduction of $86,859.75 as a loss on such preferred stock, being the difference between the amount paid by petitioner for the stock, and the amount of the liquidating distribution. Respondent disallowed the deduction because "the loss sustained in connection with the stock is held to be from an exchange of stock held less than two years" and petitioner "had no gain from sales or exchanges of assets held less than two years." Respondent relied on Sec. 23 (r) of the Revenue Act of 1932 (47 Stat. 169).

On petition to redetermine the deficiency the Board sustained respondent, holding that "this disposition of the stock, under the provisions of the statute considered above, was a sale or exchange and the deduction of the losses sustained is barred by the provisions of section 23 (r) (1)." Five members of the Board dissented. The instant petition to review the decision of the Board, entered pursuant to its holding, was then filed.

Section 21 of the act provides:

"'Net income' means the gross income computed under section 22, less the deductions allowed by section 23."

Section 22 provides in part:

"(a) 'Gross income' includes * * * income derived from * * * sales, or dealings in property * * *

"(d) Distributions by corporations shall be taxable to the shareholders as provided in section 115."

Section 23 provides in part:

"In computing net income there shall be allowed as deductions: * * *

"(f) Subject to the limitations provided in subsection (r) of this section, in the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise * * *

"(r) (1) Losses from sales or exchanges of stocks and bonds * * * which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges * * *"

Section 115 provides in part:

"(c) Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112 * * *"

We think that petitioner is entitled to the deduction by virtue of sections 22 (d), 115 (c), and 112. The amount received by petitioner was a liquidating dividend. Under section 22 (d), that dividend is taxable as provided in section 115 (c). Under the latter section, the gain or loss is to be computed under section 111 but the amount arrived at by the computation shall be recognized to the extent provided in section 112. Under section 112, the entire amount of the loss must be recognized.

Petitioner contends that the deduction is authorized by section 23 (f), and argues that the limitation in section 23 (r) (1) is not applicable. Section 23 (f) is a general statute relating to losses, whereas sections 22 (d), 115 (c), and 112 are special with respect to the particular situation. Where there are two statutes, one being a general statute, and the other being a specific statute, and both cover the same subject matter, the specific statute should control. Therefore, we think section 23 (f) should not be applied.

Respondent contends that section 23 (r) (1) prohibits the deduction. It is asserted, as the Board held, that in effect there was an exchange of the stock for money. Petitioner argues, as the dissenting opinion of the Board members points out, that the legislative history of section 23 (r) (1) was not intended to apply to such a situation as is present here. We think section 23 (r) (1) is not applicable.

First. Section 23 (r) (1) is broader and includes more transactions than sections 22 (d), and 115 (c) and 112. As compared with those sections, it again is general. The specific statute should control rather than the general statute.

Second. By its terms section 23 (r) (1) applies only to "sales or exchanges." We think the liquidating dividend here is neither, within the ordinary and accepted meaning of those terms. A "sale or exchange" implies, we think, that each party to the transaction shall obtain something. We do not believe that the Townsend company received anything. There is no inconsistency with the application of section 115 (c), because it does not say a liquidating distribution is an "exchange," but says it "shall be treated" as such for the purpose of applying sections 111 and 112. It does not say that a liquidating distribution shall be treated as an "exchange" for the purpose of section 23 (r) (1).

Third. Had there been no liquidating dividend on the stock, petitioner could have deducted the entire loss. Reg. 77, Art. 174. (Same rule applies to bonds. Art. 194.) The rule announced by the Board leads to the conclusion that a holder of $100,000 of stock who gets a liquidating dividend of ten cents, cannot deduct his $99,999.90 loss. Such construction should be avoided, we think, on the authority of United States v. Katz, 271 U. S. 354, 357, where it is said:

"All laws are to be given a sensible construction; and a literal application of a statute, which would lead to absurd consequences, should be avoided whenever a reasonable application can be given it, consistent with the legislative purpose * * *"

Fourth. The most that can be said for respondent, is that it is doubtful whether Sections 22 (d), 115 (c), and 112, on the one hand, or section 23 (r) (1) on the other hand is applicable. The rule announced in Gould v. Gould, 245 U. S. 152, 153, is applicable, we think, and is: "In case of doubt they [taxing statutes] are construed most strongly against the Government, and in favor of the citizen." Therefore, section 23 (r) (1) should be construed as not applicable to petitioner.

We believe it is unimportant, whether the "deduction may be taken in the form of a minor or negative item of gross income," as mentioned by the Board, or whether it is taken as an outright deduction.

Decision reversed.

STEPHENS, Circuit Judge, dissenting:

The Chester N. Weaver Company, the petitioner here, is a California corporation. Consolidated on review and dependent on the decision of this court upon this petition are petitions for review brought by Chester N. Weaver and Elsie S. Weaver.

On December 2, 1931, Mr. and Mrs. Weaver purchased 500 shares each of the six per cent cumulative preferred stock of the Jeff R. Townsend Company, hereinafter referred to as the Townsend Com-

pany, paying therefor $500 per share. On August 9, 1932, the Weaver Company acquired from the same corporation 1,000 shares of its preferred stock at the same price per share. The 2,000 shares of preferred stock so purchased constituted all of the preferred stock of the Townsend Company. The common stock belonged to other interests. The articles of incorporation provided that in the event of liquidation the holders of preferred stock should be entitled to receive therefor a sum equal to 105 per cent of the par value thereof before any amount should be distributed to the holders of the common stock.

Early in 1933 the Townsend Company became financially involved and unable to continue business. Its stockholders took the necessary steps to effect its dissolution and liquidation. On or about September 17, 1933, it sold all of its assets to the Weaver Company for $26,780.50. On September 18, 1933, the two Weavers and the Weaver Company, holders of all of the preferred stock of the Townsend Company, surrendered their stock certificates for cancellation and for the purpose of completing liquidation and effecting dissolution of that company. The $26,280.50 received for its assets was distributed in liquidation to the preferred stockholders pro rata. The Weaver Company received $13,140.25; Chester N. Weaver, $6,560.13, and Elsie S. Weaver, $6,570.12.

In their income tax returns for 1933 each of the stockholders deducted as a loss the difference between the amount paid for the preferred stock so surrendered and the amount received in liquidation, and, in determining the deficiencies herein, the Commissioner disallowed the deductions so claimed.

The Board of Tax Appeals held that the deductions were barred by Section 23 (r) (1) of the Revenue Act of 1932, c. 209, 47 Stat. 169, and approved the Commissioner's determination. Accordingly it decided that the deficiency due from the Weaver Company amounted to $4,323.48; that from Chester N. Weaver, $8,832.43; and that from Elsie N. Weaver, $2,447.84.

Section 23 (r) (1) provides as follows:

"Losses from sales or exchanges of stocks and bonds [as defined in subsection (t) of this section] which are not capital assets [as defined in section 101] shall be allowed only to the extent of the gains from such sales or exchanges [including gains which may be derived by a taxpayer from the retirement of his own obligations]."

Since it is not claimed by the petitioner that the surrendered stock was a capital asset or that it has non-capital gains which might offset the loss here claimed, the only question presented is whether the petitioner's act of surrendering its stock in the Townsend Company and that company's act of paying the petitioner $13,140.25 for the stock which was in complete liquidation of the company, constituted a sale or exchange of stock within the meaning of Section 23 (r) (1). If it did the decision of the Board disallowing the claimed deduction was proper.

In order to decide the question before us, it seems advisable to relate section 23 (r) to other applicable sections in the framework

of the Revenue Act. Sections 11, 12, and 13 of the Revenue Act of 1932 provide for a yearly tax upon the net income of every individual and every corporation. Section 21 provides that:

"'Net income' means the gross income computed under section 22, less the deductions allowed by section 23."

It is evident, then, that in claiming the right to take a deduction it is necessary to show that it is authorized by section 23. New Colonial Co. v. Helvering, 292 U. S. 435, 440.

Among other allowable deductions enumerated in section 23 is that set out in subsection (f):

"Losses by Corporations.—Subject to the limitations provided in subsection (r) of this section, in the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise."

It is under authority of last-quoted subsection that petitioner claims the right to deduct the difference between the amount paid for the Townsend Company stock and the amount distributed to it as a stockholder on liquidation of that corporation.[1]

It is to be noted that section 23 (f) is self-limited by section 23 (r) [which has been quoted above]. The general effect of the two subsections when taken together is that a corporation may deduct all losses it sustains, provided, however, that if a loss results from a sale or exchange of stocks or bonds it may be deducted only to the extent that the corporation has gained from such sales or exchanges.

Petitioner's position is that it suffered a loss on the liquidation of the Townsend Company and that this loss did not result from a sale or exchange of stocks or bonds, and that consequently the whole amount thereof is deductible. One branch of petitioner's argument is founded on quotations from Congressional committee reports. It is asserted that these reports show that Congress did not intend to make liquidation distributions subject to the limitations of section 23 (r). We do not think it is proper to resort to such sources, since, as will be seen, the Act itself provides the solution to the problem without extraneous aid. Moreover, the reports relied on afford, at best, merely negative evidence of the Congressional intent. The fact that the reporting committees have nowhere specifically stated that distributions on liquidation were to be treated as exchanges within the meaning of section 23 (r) is not persuasive that they intended to exclude such transactions from the operation of that section.

A second argument advanced by the taxpayer is that section 22 makes it clear that there is a distinction between a sale or exchange on one hand and a distribution in liquidation on the other. It is pointed out that subsection (d) of section 22 provides that:

"Distributions by corporations shall be taxable to the shareholders as provided in section 115."

[1] Section 23 (e) which applies to individuals, has the same effect, insofar as we are here concerned, as has 23 (f) in the case of corporations.

while in the next subsection (e) it is provided that:

"In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in sections 111, 112, and 113."

It is urged that the differentiation thus made in Section 22 between a corporate distribution and a "sale or other disposition of property" shows that a distribution on liquidation is not a "sale or exchange" within the meaning of section 23 (r). We do not find this argument persuasive—in fact the provisions thus called to our attention are in the last result influential toward a conclusion opposite to that suggested by petitioner. That such is their effect, we think, becomes clear when section 115 [to which section 22 (d) refers] is examined.

Section 115 [which is entitled "Distributions by Corporations" as is section 22 (d)] defines the term "dividend" in subsection (a); and in subsection (b) fixes the source of corporate distributions for the purposes of the Act. Subsection (c) provides in pertinent part:

"Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112."

We believe that the phrasing of this section shows an intent to settle for tax purposes the somewhat anomalous character of a liquidation distribution transaction as a sale or exchange of the stock for the amount distributed. We think this interpretation is borne out when, as directed by section 115 (c), reference is made to section 112, for that section is concerned only with the recognition of gain or loss upon "the sale or exchange of property"—if a distribution in liquidation is not fixed as a "sale or exchange" by section 115 (c) the reference therein to section 112 would be without effect.

It is further significant to note that section 23 (r) first appeared in the Revenue Act of 1932. The Revenue Act of 1928[2] contained subsections (d) and (o) of section 22 and subsection (c) of section 115 in form identical with that in which they appear in the 1932 act. Thus it appears that when subsection (r) of section 23 was enacted, distributions in liquidation had previously been impressed with the character of payments on sale or exchange. The reenactment without change of the sections characterizing liquidation distributions as exchanges, in the Act which first limited the deductibility of losses on stock sales or exchanges, is strongly indicative of the intention of Congress to include within the limitation provisions of section 23 (r) such liquidation transactions.

In addition to petitioner's contentions so far discussed another argument, or an elaboration of that just disposed of, has been advanced. Ingenious though it may be we do not consider it sound.

[2] May 29, 1928, c. 852, section 22, 115, 45 Stat. 797, 822. Substantially identical provisions were also included in the Revenue Acts of 1918, 1924, and 1926.

The elaboration is based upon the reference in section 22 (d) to section 115, which section in turn refers to sections 111 and 112. The substance of this supplemental argument is: under the reference in 115 (c) only subsection (c) of section 111 is applicable since that subsection alone deals with "exchanges," with which character 115 (c) endows distributions in liquidation; that section 111 (c) refers to section 112 for the recognition of loss in the case of an "exchange"; and that section 112 (a) [the only portion of section 112 which is applicable] provides that upon an "exchange" the entire amount of the gain or loss is to be recognized. It is not clear whether petitioner advances the foregoing argument only to bolster the contention that the Revenue Act clearly recognizes a distinction between a "distribution in liquidation" and an "exchange" or whether petitioner is claiming that losses resulting to stockholders from corporate liquidations are to be given effect through section 22 (d) without regard to the provisions of section 23. The latter interpretation was given the argument by the Board.

Since, as we see it, the statutory analysis upon which the argument proceeds is faulty it can be given no weight wherever it is intended to lead.

Section 111 (c), claimed to be the sole provision of section 111 applicable under reference from section 115 (c), does not fix the mode of determination of gain or loss [for which purpose 115 (c) refers to 111] but merely refers to section 112 for the provisions governing recognition of the loss determined under other of its own provisions. Unless then we assume that the law-making body performed a useless act when it enacted in section 115 (c) a reference to section 111, we are bound to give application to other portions of section 111 than subsection (c) thereof for 115 (c) itself refers to section 112 for recognition of loss. Again, if petitioner's argument were to be accepted the result would be that though 115 (c) distinguishes between "determination" and "recognition" of gain or loss by reference to sections 111 and 112, respectively, the net effect of the references would be the "recognition" of a gain or loss nowhere "determined." Moreover, when section 111 is read as a whole, the expression "sale or other disposition of property" used in subsections (a) and (b) thereof is seen to have been intended to cover an "exchange" for subsection (c) thereof refers to section 112 only in those instances in which there has been a determination "under this section [section 111]" of the extent of gain or loss on "a sale or exchange." There could be no determination of loss on an "exchange" under section 111 unless the phrase "other disposition of property" contained in that section is inclusive of "exchange."

Moreover, if losses on liquidation distributions are to be governed by the provisions of section 22 (d), 115 (c), 111, and 112 without regard to section 23, logic would lead to the conclusion that section 23 (r) is in no case to be given any effect. This is true because both in the case of a "distribution by a corporation" [22 (d)] and

in the case of a "sale or other disposition of property" [22 (e)] the ultimate reference is to section 111 for "Determination," and to section 112 for "Recognition" of gain or loss. If the provision of section 112 to the effect that the entire amount of gain or loss (determined under section 111) shall be "recognized" means in the case of liquidation that such loss may be deducted independent of the provisions of section 23, the same result must follow in the case of a sale of stock. And if it does follow, then section 23 (r) can be given no effect or operation. By the same token the references made in subsections (e) and (f) of section 23 to "the limitations provided in subsection (r)" would be purposeless, for the transactions limited by "subsection (r)" do not, under this view, come within the purview of 23 (e) or (f).

I conclude that the separate provision in section 22 as to distributions by corporations on one hand and sales or other dispositions of property on the other hand does not make a distinction between a distribution in liquidation and a sale or exchange such as to prevent the application of section 23 (r). On the contrary the ultimate effect of these provisions is to make it clear that such transactions are "exchanges" within the meaning of section 23 (r) and therefore subject to the limitations therein provided. The rule is long-established that the intention of the lawmaker is to be deduced from a view of every material part of a statute. Hellmich v. Hellman, 276 U. S. 233, 237. Congress having classified a transaction involving a distribution in liquidation as an exchange such classification requires it to be treated as coming within any provisions pertaining to exchanges.

It has previously been held that the provision of section 115 (c) that amounts distributed in liquidation "shall be treated as in full payment in exchange for the stock" characterizes such transactions as "exchanges" for income tax purposes. In White v. U. S. (Ct. of Clms. 1937), 21 F. Supp. 361, it was held that an amount received by a holder of preferred shares on partial liquidation of a corporation was properly treated as a "capital" rather than an "ordinary" loss, the court stating that the provisions of section 115 (c) "make a liquidating dividend have the same effect as a sale or exchange of property" and that consequently the distribution in question was a "deductible loss resulting from the sale or exchange of capital assets" within the meaning of section 101 (c) (2). See also, Eckols v. Commissioner (C. C. A. 8, 1932), 61 Fed. (2d) 191; Childs v. Commissioner, 35 B. T. A. 1125 (1937); Reg. 77, Art. 625.

The argument that section 23 (r) is not here applicable because it is broader and includes more transactions than sections 22 (d), 115 (c), and 112 and consequently should not control the last named sections, has validity only if the so-called "specific" statutes are in conflict with the so-called "broader" statutes. The statutes are not in conflict unless it is thought that sections 22 (d), 115 (c), and 112 in and of themselves allow a loss deduction by way of a minus item

of gross income. I have above suggested my reasons for thinking that they do not.

While it is true that the general rule is that acts levying taxes are, in case of doubt, to be construed in favor of the citizen, in my opinion the more specific rule applicable here is that deductions, like exemptions, are privileges, and a person claiming a deduction must point to an applicable statute and show that he comes within its terms. New Colonial v. Helvering, 292 U. S. 435, and cases cited; see also, Paul & Mertons, Law of Federal Income Taxation, Vol. I, section 330 (1937 Cum. Supp.).

The suggestion that in a stated hypothetical case a harsh result will follow from the conclusion that a distribution in liquidation is an exchange within the intendment of section 23 (r) is, I think, answered by the following quotation from Helvering v. Twin Bell Syndicate, 293 U. S. 312, 321:

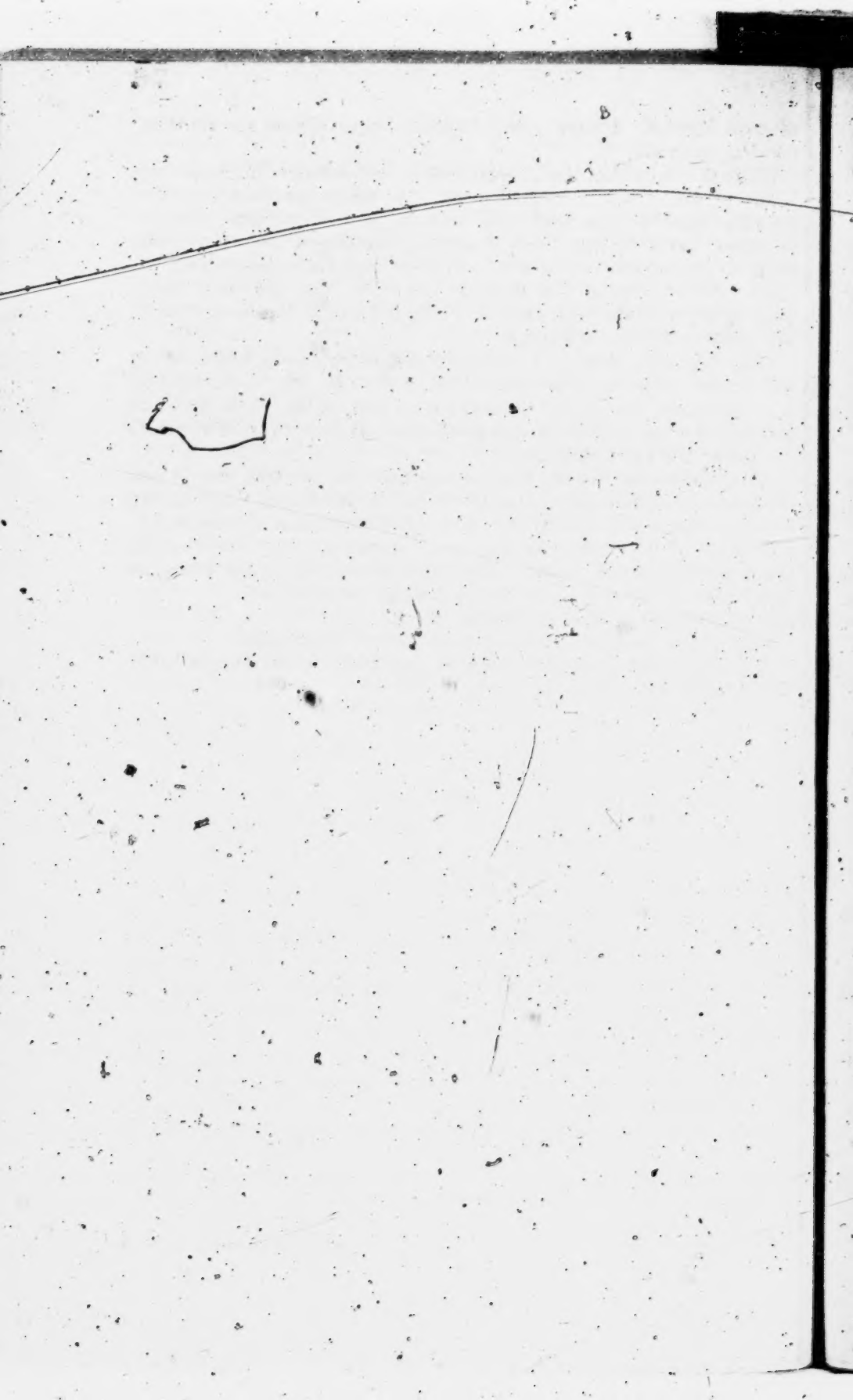
"The respondent insists that, so applied, the sections may work unjust and unequal results, but it is to be remarked that this is likely to be so wherever a rule of thumb is applied without a detailed examination of the facts affecting each taxpayer. No doubt as the petitioner points out, equally illogical results might ensue from the application of the section, as the respondent construes it."

See also, Eckols v. Commissioner, supra.

I am of the opinion that the decision should be affirmed.

[Endorsed:] Opinion and dissenting opinion. Filed June 2, 1938. Paul P. O'Brien, Clerk.

U. S. GOVERNMENT PRINTING OFFICE: 1938



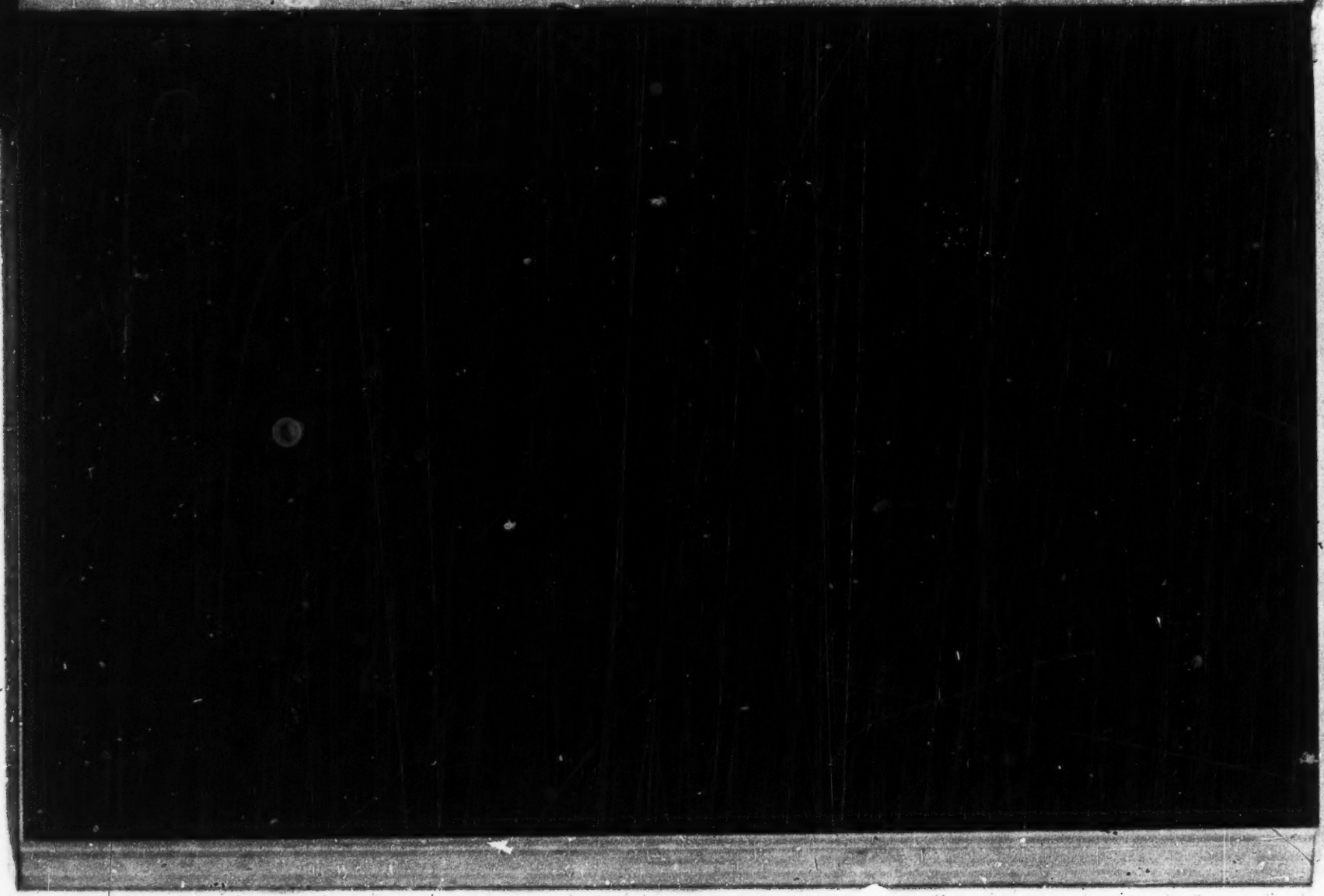
Order allowing certiorari

Filed October 10, 1938

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Ninth Circuit is granted, and the case is assigned for argument immediately following Nos. 96 and 97.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

U. S. GOVERNMENT PRINTING OFFICE 1938



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In the Supreme Court of the United States

OCTOBER TERM, 1938

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

CHESTER N. WEAVER COMPANY, A CORPORATION

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the decision of the United States Circuit Court of Appeals for the Ninth Circuit entered in the above cause on June 2, 1938 (R. 67).

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 20–38) is reported in 35 B. T. A. 514. The opinion and dissenting opinion in the Circuit Court of Appeals (R. 68–76) are reported in 97 F. (2d) 31.

JURISDICTION

The judgment of the Circuit Court of Apeals was entered on June 2, 1938 (R. 67). The jurisdiction

of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a liquidating dividend is to be treated as a sale or exchange within the meaning of Section 23 (r) (1) of the Revenue Act of 1932, which allows the deduction of losses from sales and exchanges of stocks and bonds which are not capital assets only to the extent of the gains from such sales or exchanges.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra*, pp. 8–11.

STATEMENT

Respondent, a California corporation, on August 9, 1932, purchased 1,000 shares of the preferred stock of Jeff R. Townsend Company, paying therefor $100 per share (R. 22).

Early in 1933 the Townsend Company became financially involved and unable to continue business. Its stockholders took the necessary steps to effect its liquidation and dissolution. On or about September 17, 1933, respondent purchased all the assets of the Townsend Company for $26,280.50. This sum was distributed in liquidation pro rata to the preferred stockholders of the Townsend Company. On September 18, 1933 (less than two years from the date of its purchase), respondent re-

ceived $13,140.25 of the distribution in liquidation, and surrendered its stock certificates for cancellation (R. 22–23).

In its income-tax return for 1933 respondent deducted as a loss the difference between the amount paid for the preferred stock and the amount received in liquidation (R. 23). The Commissioner disallowed the deduction, determining that the loss was sustained from an exchange of stock held less than two years, within the meaning of Section 23 (r) (1); and that respondent had no such gain against which the loss could be applied (R. 13, 23). The Board, five members dissenting, entered an order sustaining the deficiencies (R. 38–39). The Circuit Court of Appeals, Judge Stephens dissenting, reversed the decision of the Board (R. 67).

SPECIFICATION OF ERRORS TO BE URGED

The court below erred:

1. In holding that the liquidating dividend was not a sale or exchange within the purview of Section 23 (r) (1) of the Revenue Act of 1932 (c. 209, 47 Stat. 169).

2. In holding that the loss resulting from the liquidation is deductible under the provisions of Sections 22 (d), 115 (c), and 112 of the Revenue Act of 1932.

REASONS FOR GRANTING THE WRIT

1. The decision of the court below is in substantial conflict with the decision of the United States

Court of Claims in *White* v. *United States*, 21 F. Supp. 361, now pending on a petition by the taxpayer for writs of certiorari. Nos. 96, 97, October Term, 1938.

The two decisions involve different sections of the revenue laws, but in each the question at issue and the principles governing decision are identical. The *White* case involved the application of Section 101 (b) of the Revenue Act of 1923 (c. 852, 45 Stat. 791) which limits the diminution of income tax to 12½ per cent of capital net loss. The Court of Claims held that section applicable to a liquidating dividend, basing its decision on the fact that Section 101 (c) (2) of the 1928 Act defined a "capital loss" as a "deductible loss resulting from the *sale or exchange* of capital assets" (italics supplied), and that Section 115 (c)[1] provided that liquidating dividends "shall be treated as in full payment *in exchange for* the stock * * *." (Italics supplied.)

The majority of the court below refused to accept that interpretation of Section 115 (c). Section 23 (r) (1) of the 1932 Act, *infra*, p. 9, provides that "Losses from *sales or exchanges* of stocks and bonds * * * which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges * * *." (Italics supplied.) In spite of the fact that Section 115 (c) of the 1932 Act,

[1] Identical with 115 (a) of the 1932 Act.

like Section 115 (c) of the 1928 Act, directed that liquidating dividends be treated as in full payment *in exchange* for the stock, the majority refused to apply Section 23 (r). The opinion states (R. 70) that Section 115 (c) "does not say a liquidating distribution is an 'exchange,' but says it 'shall be treated' as such for the purpose of applying sections 111 and 112." As pointed out in the dissenting opinion, the effect of the decision is to allow the loss as a minus item of gross income under Section 22 (d) (dealing with gross income) and to disregard the provisions of Section 23. The decision imputes to Congress the intention to direct that a liquidating dividend be treated as a sale or exchange in computing the amount of the loss, while it is to be treated otherwise in determining the deductibility of the same loss. The dissenting judge, relying on the *White* case, reached the opposite result.

The conflict between the two decisions is undeniable. Each case turns upon the question whether distributions in liquidation are, under Section 115 (c), subject to provisions governing losses resulting from a sale or exchange of assets. The Government, believing that a conflict exists which should be resolved by this Court, is not opposing the petition for certiorari in the *White* case.[2]

[2] The Government did oppose a petition for a writ of certiorari in *Fairbanks* v. *United States*, No. 65, October Term, 1938. That case is readily distinguishable. There the question involved is whether the gain from the redemption of bonds is a sale or exchange. There is no provision in the Act there involved for so treating such redemption.

2. The court below has erroneously decided an important question of Federal law which has not been, but should be, settled by this Court. Section 115 (c), providing that amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, has been reenacted in the Revenue Acts of 1934 (c. 277, 48 Stat. 680), 1936 (c. 690, 49 Stat. 1648) and 1938 (Pub., No. 554, 75th Cong., 3d Sess.). Hence the problem whether liquidating dividends shall be treated as received upon an exchange within the meaning of sections of the statute other than those mentioned in Section 115 (c) will continue to recur. The question is, in fact, now pending before the court below in connection with the 1934 Act in *Martin General Agency* v. *Commissioner*, on appeal from the Board of Tax Appeals, whose memorandum opinion, not reported, was rendered August 19, 1937.

Furthermore, the court below has cast doubt upon the proper scope of Section 112. If, as the court held, Section 112 (similar throughout the Revenue Acts) allows the *deduction* of a loss where it simply provides that a loss is to be *recognized*, the provisions of Section 23 (r) (1), Section 101 (b), and all other provisions dealing with distributions in liquidation are rendered wholly nugatory. We submit, on the contrary, that the purpose of Section 112 is merely to distinguish between closed transactions wherein the loss is to be recognized, and transactions not closed wherein the loss is not

to be recognized. The amount of the loss is thus determined under Sections 111 and 112; its deductibility is to be determined under Section 23.

CONCLUSION

Wherefore, it is respectfully prayed that this petition for a writ of certiorari be granted.

ROBERT H. JACKSON,
Solicitor General.

AUGUST 1938.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 13. TAX ON CORPORATIONS.

(a) RATE OF TAX.—There shall be levied, collected, and paid for each taxable year, upon the net income of every corporation, a tax of 13¾ per centum of the amount of the net income in excess of the credit against net income provided in section 26.

* * * * *

SEC. 21. NET INCOME.

"Net income" means the gross income computed under section 22, less the deductions allowed by section 23.

SEC. 22. GROSS INCOME.

(a) GENERAL DEFINITION.—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

(d) DISTRIBUTIONS BY CORPORATIONS.—Distributions by corporations shall be taxable to the shareholders as provided in section 115.

(e) DETERMINATION OF GAIN OR LOSS.—In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in sections 111, 112, and 113.

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(e) LOSSES BY INDIVIDUALS.—Subject to the limitations provided in subsection (r) of this section, in the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; or

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business;

* * * * *

(f) LOSSES BY CORPORATIONS.—Subject to the limitations provided in subsection (r) of this section, in the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.

* * * * *

(r) LIMITATION ON STOCK LOSSES.—(1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

* * * * *

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) COMPUTATION OF GAIN OR LOSS.—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis

provided in section 113 (b), and the loss shall be the excess of such basis over the amount realized.

* * * * *

(c) RECOGNITION OF GAIN OR LOSS.—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) GENERAL RULE.—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section. * * *

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

(c) DISTRIBUTIONS IN LIQUIDATION.—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. * * *

Revenue Act of 1924, c. 234, 43 Stat. 253:

DISTRIBUTIONS BY CORPORATIONS

SEC. 201. * * *

(c) Amounts distributed in complete liquidation of a corporation shall be treated

as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 202, but shall be recognized only to the extent provided in section 203. * * *

U. S. GOVERNMENT PRINTING OFFICE: 1938

No. 304

In the Supreme Court of the United States

OCTOBER TERM, 1938

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

CHESTER N. WEAVER COMPANY, A CORPORATION

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE PETITIONER

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BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion and dissenting opinion in the United States Board of Tax Appeals (R. 20–38) are reported in 35 B. T. A. 514. The opinion and dissenting opinion in the Circuit Court of Appeals (R. 68–76) are reported in 97 F. (2d) 31.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on June 2, 1938 (R. 67). The petition for certiorari was filed on August 26, 1938, and was

granted on October 10, 1938. The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a liquidating dividend is to be treated as a sale or exchange within the meaning of Section 23 (r) (1) of the Revenue Act of 1932, which allows the deduction of losses from sales and exchanges of stocks and bonds which are not capital assets only to the extent of the gains from such sales or exchanges.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra*, pp. 23–29.

STATEMENT

Respondent, a California corporation, on August 9, 1932, purchased 1,000 shares of the preferred stock of Jeff R. Townsend Company for $100 a share (R. 22).

Early in 1933 the Townsend Company became financially involved and unable to continue business. Its stockholders took the necessary steps to effect its liquidation and dissolution. On or about September 17, 1933, respondent purchased all the assets of the Townsend Company for $26,280.50. This sum was distributed in liquidation pro rata to the preferred stockholders of the Townsend Company. On September 18, 1933 (less than two years from the date of purchase of the stock), re-

spondent received $13,140.25 of the distribution in liquidation, and surrendered its stock certificates for cancellation (R. 22–23).

In its income-tax return for 1933 respondent deducted as a loss the difference between the amount paid for the preferred stock and the amount received in liquidation (R. 23). The Commissioner disallowed the deduction, determining that the loss was sustained from an exchange of stock held less than two years, within the meaning of Section 23 (r) (1); and that respondent had no such gain against which the loss could be applied (R. 13, 23). The Board, five members dissenting, entered an order sustaining the deficiencies (R. 38–39). The Circuit Court of Appeals, Circuit Judge Stephens dissenting, reversed the decision of the Board (R. 68–76).

SPECIFICATION OF ERRORS TO BE URGED

The court below erred:

1. In holding that the liquidating dividend was not a sale or exchange within the purview of section 23 (r) (1) of the Revenue Act of 1932 (c. 209, 47 Stat. 169).

2. In holding that the loss resulting from the liquidation is deductible under the provisions of sections 22 (d), 115 (c), and 112 of the Revenue Act of 1932.

SUMMARY OF ARGUMENT

I. Section 23 (r) (1) of the Revenue Act of 1932, limiting the deduction of losses on "sales or ex-

changes of stocks and bonds" to the extent of gains from such exchanges, in the absence of such gains in the present case bars the deduction of the loss upon the corporate liquidation. Under section 115 (c), providing that the amount distributed to the taxpayer in the liquidation shall be treated as in exchange for the taxpayer's stock, the liquidation is in effect a sale or exchange of the stock within section 23 (r) (1). The legislative history of section 23 (r) (1) does not support the taxpayer's contention that a corporate liquidation is not a sale or exchange of stock within section 23 (r) (1).

II. The loss is not deductible in virtue of sections 22 (d), 115 (c), and 112 without reference to section 23 (r) (1). These sections merely determine the amount of the loss which is to be "recognized" and do not determine the additional question whether the loss is deductible. Under section 23 (r) (1) the loss is not deductible.

ARGUMENT

THE DEDUCTION OF THE TAXPAYER'S LOSS UPON THE CORPORATE LIQUIDATION IN 1933 IS PROHIBITED BY SECTION 23 (r) (1) OF THE REVENUE ACT OF 1932

On August 9, 1932, the taxpayer, a corporation, purchased 1,000 shares of the preferred stock of another corporation for $100,000. On September 18, 1933, less than two years later, the taxpayer surrendered the certificates of preferred stock for cancellation and received $13,140.25 in the complete liquidation of the other corporation. The tax-

payer deducted the resulting loss of $86,859.75 from gross income in its 1933 income tax return (R. 6–7).

The Commissioner of Internal Revenue (R. 9) and the Board of Tax Appeals, five members dissenting (R. 20–38), determined that deduction of such a loss is limited by section 23 (r) (1) of the Revenue Act of 1932 to the extent of offsetting gains, and since there were no such gains disallowed the loss and determined a deficiency of $4,323.48. The court below held, Circuit Judge Stephens dissenting (R. 68–76), that the loss is deductible. The petition for certiorari granted October 10, 1938, asserts a conflict with *White* v. *United States*, 21 F. Supp. 361 (C. Cls.), certiorari granted October 10, 1938, Nos. 96 and 97, present Term, to be argued immediately before this case.

The petitioner contends that deduction of the loss (I) is barred by section 23 (r) (1) and (II) is not allowed, as the court below held, "by virtue of sections 22 (d), 115 (c), and 112" (R. 69).

I

SECTION 23 (r) (1) BARS THE DEDUCTION

The taxpayer is a corporation. Section 13 of the 1932 Act levies a tax for each taxable year upon the net income of every corporation. Section 21 provides:

> "Net income" means the gross income computed under section 22, less the deductions allowed by section 23.

Consequently, the petitioner contends, the taxpayer may deduct from gross income only those deductions allowed by Section 23. Moreover, "only as there is clear provision therefor can any particular deduction be allowed." *New Colonial Co.* v. *Helvering*, 292 U. S. 435, 440.

The respondent in its brief in the court below relied upon section 23 (f) as the statutory authority for the deductions and, although section 23 (f) by its terms is limited by section 23 (r), contended that section 23 (r) (1) does not apply to corporate liquidations. The petitioner contends that section 23 (r) (1) does apply to corporate liquidations and prohibits the deduction.

Section 23 provides:

> In computing net income there shall be allowed as deductions:
>
> * * * * *
>
> (f) *Losses by corporations.*—Subject to the limitations provided in subsection (r) of this section, in the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.
>
> * * * * *
>
> (r) *Limitation on stock losses.*—
>
> (1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101), shall be allowed only to the extent of the gains from such sales or exchanges (including gains

which may be derived by a taxpayer from the retirement of his own obligations).

* * * * * *

(t) *Definition of stocks and bonds.*—As used in subsections (r) and (s), the term "stocks and bonds" means (1) shares of stock in any corporation, * * *.

Section 101 (c) (8) provides:

"Capital assets" means property held by the taxpayer for more than two years * * *.

The petitioner contends (1) that the claimed deduction is prohibited by the words of section 23 (r) (1); (2) that the language of section 23 (r) (1) so clearly denies the claimed deduction that recourse to its legislative history is not proper or necessary; (3) that the legislative history of the section supports the petitioner's construction; and (4) that the petitioner's construction does not produce a harsh result.

1. *The terms of section 23 (r) (1) forbid the deduction*

Section 23 (f), the statutory authority for the deduction relied upon by the respondent in its brief in the court below, by its own terms is expressly subject to the limitations of section 23 (r). Consequently, the deduction cannot be allowed if it is prohibited by section 23 (r) (1).

Concededly, the stock was held by the taxpayer for less than two years and, therefore, was not

capital assets. It is not denied that the taxpayer in 1933 did not have gains from sales or exchanges of stock or bonds which were not capital assets to the extent of which the claimed deductions would have been allowed by section 23 (r) (1). This section applies, therefore, if the exchange of the taxpayer's stock for the liquidating dividend in cash is within the phrase "sales or exchanges of stocks" in section 23 (r) (1).

The petitioner contends that exchanges of stock in liquidation are in effect, and in virtue of section 115 (c), "sales or exchanges of stocks" within section 23 (r) (1). The petitioner's construction is supported by (a) section 115 (c); (b) the judicial decisions, applying section 115 (c), which determine that exchanges of stock in corporate liquidations are sales or exchanges of stock; (c) the clear understanding of Congress that section 115 (c) treats corporate liquidations as a "sale of stock"; and (d) the treatment of liquidations as sales of stock, applying section 115 (c) under sections of the revenue acts other than section 23 (r) (1).

a. Section 115 (c) provides in part:

> (c) *Distributions in liquidation.*—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under

> section 111, but shall be recognized only to the extent provided in section 112. * * *

In these plain terms section 115 (c) provides that amounts distributed shall be treated as payment in exchange for stock. The petitioner contends that where, as here, the amount distributed is cash there is a sale of the stock within the phrase "sales or exchanges" in section 23 (r) (1).

b. The decisions, applying section 115 (c), hold that corporate liquidations shall be treated as what they in effect are—sales of stock to the corporations in liquidation, taxable in like manner as if the stockholders had sold their stock to third persons. *Hellmich* v. *Hellman*, 276 U. S. 233, 237; *Langstaff* v. *Lucas*, 9 F. (2d) 691, 694 (W. D. Ky.), affirmed 13 F. (2d) 1022 (C. C. A. 6th), certiorari denied, 273 U. S. 721.

In the *Hellmich* case this Court held that amounts distributed in liquidation to stockholders out of earnings after February 28, 1913, were not "dividends" under section 201 (a) of the 1918 Act exempt from the normal tax, but were payments in exchange for stock under section 201 (c), similar to section 115 (c) of the 1932 Act, subject to the normal tax. The opinion of the Court by Mr. Justice Sanford states at page 237:

> The gains realized by the stockholders from the distribution of the assets in liquidation were subject to the normal tax in like manner as if they had sold their stock to third persons.

In the *Langstaff* case the District Court, reaching the same result which this Court later reached in the *Hellmich* case, said at page 694:

> This section [201 (c) of the 1918 Act] strips distributions made to stockholders in liquidation of a corporation of all disguises and declares that they shall be considered for what they in effect are—purchases of all their outstanding stock by the liquidating corporations, and not dividends as generally understood, and as defined in section 201, subsection (a), and as used in section 216.

The Circuit Court of Appeals affirmed upon the reasoning of the District Judge and stated (13 F. (2d) 1022) that the amount distributed in liquidation "became the proceeds of the sale of Langstaff's stock in the corporation, instead of a corporate dividend."

It is submitted, therefore, that for tax purposes liquidations are in effect "sales or exchanges" of stock within the meaning of that phrase throughout the revenue acts and in section 23 (r) (1). Nothing in the language of section 23 (r) (1) indicates that the phrase has a different or more restricted meaning than that required by section 115 (c).

c. The provision of section 115 (c) requiring amounts distributed in liquidation to be treated as payments in exchange for the stock first appeared in section 201 (c) of the Revenue Act of 1918, and

has been repeated in section 201 (c) of the Acts of 1924 and 1926 and section 115 (c) of the 1928 Act and subsequent Acts [1] Congress has always considered that section 115 (c) "treats a liquidating dividend as a sale of stock, * * *."[2]

This treatment of corporate liquidations as a sale of stock supports the petitioner's view that the corporate liquidation in this case was a sale of stock within the meaning of section 23 (r) (1).

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[1] The Revenue Acts of 1921, 1917, 1916, and 1913, make no specific provision for liquidating dividends. *Lynch* v. *Turrish*, 247 U. S. 221; *Lynch* v. *Hornby*, 247 U. S. 339, 343–346; Magill, *The Income Tax Liability of Dividends in Liquidation*, 23 Mich. Law Rev. 565, 569 (1925).

[2] The Senate Committee on Finance (Rep. No. 398, 68th Cong., 1st Sess.) used this language in speaking of the section of the bill which became section 201 (c) of the Revenue Act of 1924, the predecessor of section 115 (c) of the 1928 and subsequent Acts, and stated at page 11:

"* * * The bill treats a liquidating dividend as a sale of the stock, with the result that the gain to the taxpayer is treated not as a dividend subject only to the surtax but as a gain from the sale of property which may be treated as a capital gain. The treatment of liquidating dividends under the bill is substantially the same as provided for in the revenue act of 1918. A liquidating dividend is, in effect, a sale by the stockholder of his stock to the corporation; he surrenders his interest in the corporation and receives money in place thereof. Treating such a transaction as a sale and within the capital gain provisions is consistent with the entire theory of the act and, furthermore, is the only method of treating such distributions which can be easily administered."

A similar statement is made by the Ways and Means Committee of the House (Rep. No. 179, 68th Cong., 1st Sess., p. 11) with respect to section 201 (c) of the 1924 Act.

Indeed, liquidations were so clearly treated as sales of stock under the 1932 and prior Acts, taxable as capital transactions within the phrase "sale or exchange of capital assets" in section 101 (c) of the 1932 and prior Acts, that when Congress wished to change this rule, in view of the use of liquidations as a device to avoid surtaxes on corporate distributions, it was required to add expressly to section 115 (c) of the 1934 Act the limitation that "Despite section 117 (a) [the capital gains and losses section in that Act comparable to section 101 of the former Acts] 100 per centum of the gain so recognized shall be taken into account in computing net income." The Report of the Senate Committee on Finance (Rep. No. 558, p. 37, 73d Cong., 2d Sess., Appendix, *infra*, p. 29) discussing the change, recognized that under the 1932 Act a liquidation was treated in the same manner as a sale of stock in which gain was taxable at the capital gain rate and loss was correspondingly limited, if the shareholder had held the stock for more than two years.

d. Finally, corporate liquidations have been treated as sales or exchanges of stock under sections of the revenue acts other than section 23 (r) (1). Redemption of preferred stock, held more than two years and considered as a partial liquidation under section 115 (f) of the 1932 Act and as an exchange within section 115 (c), has been held to be within the phrase "sale or exchange of capital assets" within section 101 (c) (1) and, therefore,

taxable as a capital gain rather than as an ordinary gain. *Mary S. Childs* v. *Commissioner*, 35 B. T. A. 1125, 1127. In *Martin General Agency* v. *Commissioner*, 36 B. T. A. 1328, the Board held in an unreported memorandum decision (1937 Prentice-Hall Federal Tax Service Vol. 1, Par. 271, p. 258) that a corporate liquidation was within the phrase "sale or exchange of capital assets" in section 23 (j) of the 1934 Act.[3] See also *White* v. *United States*, 21 F. Supp. 361 (C. Cls.), certiorari granted October 10, 1938, Nos. 96 and 97, Present Term, which treats a corporate liquidation as a sale or exchange of capital assets within section 101 (c) of the 1928 Act.

Nothing in the terms of the statute indicates that a liquidation which is treated as a sale of stock under section 115 (c) and is the sale of stock for income tax purposes generally is not within the same phrase "sales or exchanges of stocks" in section 23 (r) (1).

The petitioner submits that the treatment of a corporate liquidation as the sale or exchange of stock both under section 115 (c) and under the decisions applying section 115 (c) requires the conclusion that the liquidation in this case is a sale of stock within the term "sales or exchanges of stocks" in section 23 (r) (1).

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[3] This case is pending, argued but undecided, in the Ninth Circuit Court of Appeals, awaiting decision in the instant case.

2. *The long accepted meaning of the words used in section 23 (r) (1) makes unavailable reference to the legislative history of that section*

The words "sales or exchanges of stocks" since 1924 had been understood clearly to include exchanges of stock in corporate liquidations when they were used in section 23 (r) (1) of the 1932 Act. Where there can be no doubt of the meaning of the words used, reference to the legislative history of the tax statute is not available. *Helvering* v. *City Bank Co.*, 296 U. S. 85, 89. This rule applies with particular force in the present situation where the phrase to be construed, "sales or exchanges of stocks", has long been considered to include exchanges of stock in corporate liquidations.

3. *The legislative history of section 23 (r) (1) does not support the taxpayer's contention.*

Even if the words of section 23 (r) (1) were not too plain to permit recourse to legislative history, as the petitioner contends, that history does not support the taxpayer's contention that Congress did not intend to include losses in corporate liquidations within "sales or exchanges of stocks". The dissenting opinion in the Board seems to have been based solely on this ground (R. 32–38). The opinion of the court below does not seem to place any reliance, expressly at least, upon this ground (R. 70).

The petitioner contends (a) that the express statutory exceptions to section 23 (r) forbid further exceptions by implication and (b) that the classification of non-capital assets, assets held for two years or less, adopted in section 23 (r), requires the conclusion that all sales or exchanges of stocks held for two years or less, including such sales or exchanges in corporate liquidations, are included.

a. Section 23 (r) expressly exempts transactions by dealers in securities in the ordinary course of their business and transactions by banks and trust companies, or persons carrying on a banking business, in the ordinary course of such banking business. Further relief from the operation of section 23 (r) (1) was given by adding section 23 (r) (2) which permitted a limited carry-over of losses to the succeeding taxable year. A provision, section 23 (s) of the bill in the House, limiting losses on sales or exchanges of stocks and bonds which were capital assets in the same manner as such exchanges of non-capital assets, was eliminated in the Senate. The petitioner submits that the existence of these express limitations on the operation of section 23 (r) (1) indicates that Congress did not intend additional limitations by implication, such as the taxpayer seeks. *Moore Ice Cream Co.* v. *Rose*, 289 U. S. 373, 377.

b. The dissenting members of the Board apparently relied upon reference in the committee reports to sales or exchanges "in the stock and bond markets" and to "preventing speculative losses."

At the most these references indicate that one purpose of Congress was to limit losses on speculative transactions. The method adopted, however, to accomplish this purpose was not by limiting losses on sales in markets or speculative losses as such but by limiting losses on sales or exchanges of stocks and bonds held for two years or less. The reference in the House Report to "losses sustained in the stock and bond markets" is followed immediately by a statement that section 23 (r) provides a limitation upon "losses from the sale or exchange of stocks and bonds held for less than two years."[4] A limitation on losses from sales or exchanges of stocks and bonds held for less than two years was the method chosen to accomplish the purpose of Congress.

The Report of the Senate Finance Committee, discussing the elimination of Section 23 (s) of the bill which limited losses even on securities held for

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[4] Report of the House Ways and Means Committee (Report No. 708, 72nd Cong., 1st Sess., pp. 12–13) states: "Many taxpayers have been completely or partially eliminating from tax their income from salaries, dividends, rents, etc., by deducting therefrom losses sustained in the stock and bond markets, with serious effect upon the revenue. Your committee is of the opinion that some limitation ought to be placed on the allowance of such losses.

"Subsection (r) provides that losses from the sale or exchange of stocks and bonds held for less than two years shall be deductible only to the extent of the gains from sales or exchanges of such securities. The same rule is applied by subsection (s) to losses from stocks and bonds held for more than two years."

more than two years, stated that such securities have been in the hands of investors and under the existing law were subject to sufficient limitation but that transactions in stocks and bonds held for two years or less "which obviously comprise the bulk of speculative transactions" were in a somewhat different situation and the losses should be limited.[5]

Thus Congress chose the practical classification based on the length of time the securities were held to distinguish "probable investment income

[5] The Report of the Senate Finance Committee (Report No. 665, 72nd Cong., 1st Sess.) states at p. 10:
"Securities held for more than two years have been in the hands of investors."

The Report continues at p. 17:

"Your committee, while in general agreement with the purpose of the House bill, believes that the method adopted to carry out this purpose is somewhat too drastic in that it penalizes pure investment losses as well as mere speculative losses.

"As now drafted the limitation that losses on stocks and bonds can only be taken to the extent of gains from similar transactions is confined to the sale of such securities which have been held for two years or less. Gains or losses arising from the sale of stocks or bonds held for over two years are in all cases treated precisely as under present law whether such losses are incurred by a corporation or an individual. * * * Further limitation appears unnecessary in view of the above and because of the fact that these transactions are usually non-speculative in character.

"The method recommended by your Committee in dealing with transactions in stocks and bonds held for two years or less, which obviously comprise the bulk of speculative transactions, may be stated as follows: The excess of losses over gains in these transactions is not allowed as a deduction against other income, * * *.

and losses and probable speculative income and losses * * *." *Davis* v. *United States*, 87 F. (2d) 323, 325 (C. C. A. 2nd). No attempt was made to exclude all transactions not in fact speculative although involving assets held less than two years. Certainly it was not intended that losses on such transactions should be subject to no limitation when even losses on assets held for more than two years are limited.

The reference to stock and bond markets in the committee reports was merely a recognition of one of the methods in which such losses can be realized, and does not purport or intend to exclude other methods. Indeed, sales on stock and bond markets, available for the stock and bonds of large corporations, is normally not available for stock of relatively small corporations, such as the corporation liquidated in this case, which must be sold privately or liquidated to realize the loss.

Certainly, the reference to stock and bond markets in the committee report does not exclude private sales of stock from section 23 (r) (1). Equally, it is no reason for excluding exchanges of stock for liquidating dividends.

4. *The petitioner's construction does not involve a harsh or absurd result*

The court below stated that the petitioner's construction of section 23 (r) (1) should be avoided on the ground that it limits the deduction of the loss if there is any liquidating dividend, although if there were no liquidating dividend, and the stock

were worthless, the entire loss could be deducted (R. 70). The petitioner submits (a) that the different treatment of stocks exchanged for liquidating dividends and worthless stocks does not establish that the former are incorrectly treated, and (b) that the general rule cannot be modified to meet a supposed harsh result in a stated hypothetical case.

a. The fact that the deduction of the loss from worthless securities is not limited does not indicate that the statute should not be construed as limiting the loss in this entirely different situation where the securities are not worthless and are in fact exchanged for a liquidating dividend. Indeed, the treatment of worthless securities as a loss from the sale or exchange of capital assets under section 23 (k) (2) of the Revenue Act of 1938 indicates that the asserted unequal treatment of liquidating dividends and worthless securities was due to the failure to treat worthless securities as a sale or exchange rather than the failure to treat exchange of stocks in corporate liquidations like worthless securities under former acts.

b. The suggestion that in a stated hypothetical case a harsh or illogical result will follow from the conclusion that a distribution is an exchange within the intendment of section 23 (r) is answered by the decision of this Court in *Helvering* v. *Twin Bell Syndicate*, 293 U. S. 312, 321. Cf. *Lang* v. *Commissioner*, 289 U. S. 109, 113; *Echols* v. *Commissioner*, 61 F. (2d) 191, 192–194 (C. C. A. 8th). Equally illogical results will ensue from the application of

the section, as the respondent construes it. The holder of stock purchased for $100,000 (held less than two years) who sells it for ten cents can deduct his loss of $99,999.90 only to the extent of similar gains, while, under the decision below, if the ten cents were received as a liquidating dividend, he could deduct the loss. Again, one who has a gain of $100,000 upon the sale of a capital asset may be taxed at 12½%, while under the decision below, if the gain results from a liquidation and, therefore, is not gain from the "sale or exchange of capital assets," it must be returned at the normal and surtax rates—rates up to a total of 63%.

II

THE LOSS IS NOT DEDUCTIBLE UNDER SECTIONS 22 (d), 115 (c), AND 112

The Circuit Court of Appeals held (R. 69)—

> We think that petitioner is entitled to the deduction by virtue of sections 22 (d), 115 (c), and 112. The amount received by petitioner was a liquidating dividend. Under section 22 (d), that dividend is taxable as provided in section 115 (c). Under the latter section the gain or loss is to be computed under section 111 but the amount arrived at by the computation shall be recognized to the extent provided in section 112. Under section 112 the entire amount of the loss must be recognized.

As pointed out in the dissenting opinion of Judge Stephens (R. 73–75), this holding not only violates the fundamental rule that the Congressional intent

is to be gathered from the structure and plan of the statute as a whole, but also renders the loss provisions of section 23, and other sections of the statute wholly nugatory.

1. Sections 11, 12, and 13 of the Revenue Act of 1932 levy a tax for each taxable year upon the net income of every individual and every corporation. Section 21 provides that: "Net income means the gross income computed under section 22, less the deductions allowed by section 23." It is evident, therefore, that to support the right to take a deduction it is necessary to show it is authorized by section 23. *New Colonial Co.* v. *Helvering*, 292 U. S. 435, 440.

The sections relied upon by the majority of the court below do not permit deduction of a loss. Section 22 (d) (Appendix, *infra*, p. 23) deals solely with the ascertainment of gross income. Section 115 (c) (Appendix, *infra*, p. 28) provides that amounts distributed in liquidation shall be treated as in "full payment in exchange for the stock" and that the gain or loss "resulting from such exchange" shall be determined under section 111, but "shall be recognized only to the extent provided in section 112." Hence, the purport of the decision below is to allow the loss under section 22 (d) as a *minus* item of gross income, or under section 112 because it is there "recognized." The view that Congress intended to allow a deduction under a section directed to the computation of gross income to the exclusion of the section devoted to deductions seems clearly untenable. This view violates the

rule that the meaning of the statute is to be determined from its provisions as a whole (*Hellmich v. Hellman*, 276 U. S. 233, 237) and the rule that, if possible, the statute is to be construed to render all of its provisions operative.

2. Nor is "recognition" of a loss under Section 112 in any sense a determination that the loss is deductible. That section deals with exchanges in connection with a "reorganization," as defined in the statute, and other non-taxable exchanges. Its purpose is merely to determine whether a gain or loss is to be recognized for tax purposes at the time of a particular transaction or whether recognition is to be postponed in whole or in part. If a loss is recognized the question remains whether it is deductible under section 23. Otherwise, even a loss on a sale to a third person would not be limited. In the present case section 23 (r) (1) bars the deduction.

CONCLUSION

The decision below is clearly erroneous and should be reversed.

Respectfully submitted.

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NOVEMBER 1938.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 13. TAX ON CORPORATIONS.

(a) *Rate of tax.*—There shall be levied, collected, and paid for each taxable year upon the net income of every corporation, a tax of 13¾ per centum of the amount of the net income in excess of the credit against net income provided in section 26.

* * * * * *

SEC. 21. NET INCOME.

"Net income" means the gross income computed under section 22, less the deductions allowed by section 23.

SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit or gains or profits and income derived from any source whatever. * * *

* * * * * *

(d) *Distribution by corporations.*—Distributions by corporations shall be taxable to the shareholders as provided in section 115.

*

(e) *Determination of gain or loss.*—In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in sections 111, 112, and 113.

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * * *

(e) *Losses by individuals.*—Subject to the limitations provided in subsection (r) of this section, in the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; or

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business;

* * * * * *

(f) *Losses by corporations.*—Subject to the limitations provided in subsection (r) of this section, in the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.

* * * * * *

(r) *Limitation on stock losses.*—(1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

* * * * * *

SEC. 101. CAPITAL NET GAINS AND LOSSES.

(a) *Tax in case of capital net gain.*—In the case of any taxpayer, other than a corporation, who for any taxable year derives a

capital net gain (as hereinafter defined in this section), there shall, at the election of the taxpayer, be levied, collected, and paid, in lieu of all other taxes imposed by this title, a tax determined as follows: A partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner as if this section had not been enacted and the total tax shall be this amount plus 12½ per centum of the capital net gain.

(b) *Tax in case of capital net loss.*—In case of any taxpayer, other than a corporation, who for any taxable year sustains a capital net loss (as hereinafter defined in this section), there shall be levied, collected, and paid, in lieu of all other taxes imposed by this title, a tax determined as follows: a partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner as if this section had not been enacted, and the total tax shall be this amount minus 12½ per centum of the capital net loss; but in no case shall the tax of a taxpayer who has sustained a capital net loss be less than the tax computed without regard to the provisions of this section.

(c) *Definitions.*—For the purposes of this title—

(1) "Capital gain" means taxable gain from the sale or exchange of capital assets consummated after December 31, 1921.

(2) "Capital loss" means deductible loss resulting from the sale or exchange of capital assets.

(3) "Capital deductions" means such deductions as are allowed by section 23 for the purpose of computing net income, and are properly allocable to or chargeable against capital assets sold or exchanged during the taxable year.

(4) "Ordinary deductions" means the deductions allowed by section 23 other than capital losses and capital deductions.

(5) "Capital net gain" means the excess of the total amount of capital gain over the sum of (A) the capital deductions and capital losses, plus (B) the amount, if any, by which the ordinary deductions exceed the gross income computed without including capital gains.

(6) "Capital net loss" means the excess of the sum of the capital losses plus the capital deductions over the total amount of capital gain.

(7) "Ordinary net income" means the net income, computed in accordance with the provisions of this title, after excluding all items of capital gain, capital loss, and capital deductions.

(8) "Capital assets" means property held by the taxpayer for more than two years (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale in the course of his trade or business. For the purposes of this definition—

(A) In determining the period for which the taxpayer has held property received on an exchange there shall be included the period for which he held the property exchanged, if under the provisions of section 113, the property received has, for the purpose of determining gain or loss from a sale or exchange, the same basis in whole or in part in his hands as the property exchanged.

(B) In determining the period for which the taxpayer has held property however ac-

quired there shall be included the period for which such property was held by any other person, if under the provisions of section 113, such property has, for the purpose of determining gain or loss from a sale or exchange, the same basis in whole or in part in his hands as it would have in the hands of such other person.

(C) In determining the period for which the taxpayer has held stock or securities received upon a distribution where no gain is recognized to the distributee under the provisions of section 112 (g) of this Act or the Revenue Act of 1928, there shall be included the period for which he held the stock or securities in the distributing corporation prior to the receipt of the stock or securities upon such distribution.

(D) In determining the period for which the taxpayer has held stock or securities the acquisition of which (or the contract or option to acquire which) resulted in the nondeductibility (under section 118 of this Act or the Revenue Act of 1928, relating to wash sales) of the loss from the sale or other disposition of substantially identical stock or securities, there shall be included the period for which he held the stock or securities the loss from the sale or other disposition of which was not deductible.

(d) *Collection and payment of tax.*—The total tax determined under subsection (a) or (b) shall be collected and paid in the same manner, at the same time, and subject to the same provisions of law, including penalties, as other taxes under this title.

* * * * * *

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the

gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b), and the loss shall be the excess of such basis over the amount realized.

* * * * *

(c) *Recognition of gain or loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section. * * *

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

(c) *Distributions in liquidation.*—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. * * *

Revenue Act of 1924, c. 234, 43 Stat. 253:

DISTRIBUTIONS BY CORPORATIONS

SEC. 201. * * *

(c) Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock,

and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 202, but shall be recognized only to the extent provided in section 203. * * *

Report of the Committee of Finance of the Senate (Rep. No. 558, 73d Cong., 2d Sess., p. 37):

> Under existing law, a distribution in liquidation of a corporation is treated in the same manner as a sale of stock. This rule has serious objections, as it permits wealthy stockholders to escape surtax upon corporate earnings or profits distributed in the form of liquidating dividends. For instance, a corporation may have a surplus of $1,000,000. If the surplus is distributed as an ordinary dividend, it is subject to the surtax rates in the hands of the shareholders. If it is distributed as a liquidating dividend, it is subject only to the flat capital gain rate of 12½ percent in case the shareholder has held his stock for more than 2 years.

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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1938

No. 304

GUY T. HELVERING, Commissioner of Internal Revenue,
Petitioner,

vs.

CHESTER N. WEAVER COMPANY (a corporation),
Respondent.

BRIEF ON BEHALF OF RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

Respondent, Chester N. Weaver Company, in response to petition for writ of certiorari submits this brief in opposition to the granting of such a writ.

JURISDICTION.

Petitioner invokes jurisdiction under Section 240(a) of the Judicial Code (28 U.S.C. Sec. 347), but this Court has

uniformly declined to entertain jurisdiction under circumstances similar to those relied upon by petitioner.

RESTATEMENT OF QUESTION PRESENTED.

Is Section 23(r)(1) of the Revenue Act of 1932 (c. 209, 47 Stat. 169) applicable to a single distribution in complete liquidation of the assets of an insolvent corporation to its "preferred stockholders"?

DENIAL OF PETITIONER'S REASONS FOR GRANTING WRIT.

Neither lack of uniformity of decision nor important question of public interest is here involved.

This Court holds that jurisdiction to bring up cases by certiorari from Circuit Courts of Appeals was given for two purposes: first, to secure uniformity of decision between *such Appellate Courts* in the several circuits; and second, to bring up cases involving questions of importance which it is in the public interest to have decided by a court of last resort. It was not conferred merely to give another hearing to the party defeated in the Circuit Court of Appeals.

Magnum Import Co. v. Houbigant, Inc., 262 U.S. 159, 163, 43 S. Ct. 531, 532;

Forsyth v. Hammond, 166 U.S. 506, 514-515, 17 S. Ct. 665, 668.

Petitioner asserts conflict of decision herein solely with that of the Court of Claims in *White v. United States*,

21 Fed. Supp. 361, and erroneous decision of "an important question of Federal law", as the sole reasons for granting the writ. (Pet. pp. 4-6.) Neither is tenable.

1. The Court of Claims is not an appellate court. It is, in some aspects, a mere fact-finding body for the Congress and various governmental departments. It is, at most, a trial court of limited jurisdiction. It cannot be classed with Circuit Courts of Appeals, which were created for the purpose of relieving this Court from an overburden of appellate work.

> *Forsyth v. Hammond,* 166 U.S. 506, 511-513, 17 S. Ct. 665, 667.

No decision by it can raise a conflict with a decision of a Circuit Court of Appeals, as "conflict" is used in this Court's rules and decisions. Section 23(r)(1) was not contained in the 1928 Act (involved in the *White* case), or in the 1934 Act (involved in the *Martin General Agency* case, cited on page 6 of petition).

On the question presented to this Court by petitioner (Pet., p. a) and as restated by respondent (*supra,* p. 2) there is no conflict with the decision in the *White* case. Section 23(r)(1) of the Revenue Act of 1932 (c. 209, 47 Stat. 169) did not exist in the Revenue Act of 1928 (c. 852, 45 Stat. 791) which is involved in the *White* case and was abandoned by the Revenue Act of 1934 (c. 277, 48 Stat. 680). There is no parallel to Section 23(r)(1) in either the 1928 or 1934 Acts. As the statute of limitations has now run against all deficiencies arising under the 1932 Act and as there are no discoverable cases involving Section 23(r)(1) now pending hearing or decision before

either the Board of Tax Appeals or any of the Courts, it would appear that petitioner is attempting to resurrect a principle for consideration by this Court on alleged conflict with a now non-existent section of a statute.

As a conclusion to its plea for a writ on ground of conflict, respondent asserts that, because it believes a conflict to exist, it is not opposing petition for the certiorari in the *White* case. (Pet., p. 5.) The Government's consent or opposition to such petition will in no way influence this Court in the present proceeding.

It should be noted that the petition presents no Federal question in any way probably in conflict with applicable decisions of this Court.

2. There is no "important question" here presented. Petitioner has presented no other decision involving the identical question now before the Court and our research has revealed none. In the absence of such litigation and because actions under the 1932 Act are now barred it is impossible that there can be here presented a question of importance to the public.

Respondent seeks to inject a doubt upon the direct interpretation of Section 23(r)(1) of the 1932 Act by the Court below by injecting the question as to the proper scope of Section 112 of that Act and the Act of 1934. A reading of the opinion of the Court herein involved (R., p. 70) shows that the decision was based entirely upon an interpretation of Section 23(r)(1) and that respondent's injection of Section 112 of the Revenue Act of 1932 (c. 209, 47 Stat. 169) to enlarge the application of Section 23(r)(1) was cast aside.

As Section 101 of the Revenue Act of 1928 (c. 852, 45 Stat. 791), the interpretation of which is involved in the *White* case, and Section 117 of the Revenue Act of 1934 (c. 277, 48 Stat. 680), involved in the *Martin General Agency* case, are not the parallels of Section 23(r)(1) in any way and are not limited to specific classes of property nor discriminatory and restricted in the segregation of particular assets as in Section 23(r)(1), the "important question of Federal law" which petitioner seeks to have this Court settle in this case is moot. That important question can be settled as to living statutes in the *White* case, but should not be settled upon dead statutes in this case.

As no other case affecting the identical question involved in this proceeding has been presented by petitioner it would appear that no legal principle, the settlement of which would be of importance to the public, is herein involved. Hence the petition should be denied.

Layne & Bowler Corp. v. Western Well Works, 261 U.S. 387, 393, 43 S. Ct. 422, 423.

3. We direct attention of the Court to the fact that petitioner does not urge or disclose any other reason contemplated by Rule 38-5(b) of this Court which would warrant the issuance of the writ sought.

ARGUMENT.

We restate the question before this Court to emphasize that there is no dividend involved, and that Section 23(r)(1), a *general* statute, deals only with *sales and*

exchanges as such, and not with liquidations, which have none of the qualities of sales or exchanges, and which are governed by the *specific* statute, Section 115(c). There is nothing in Section 115(c) to indicate that a liquidating distribution was intended to be treated as an exchange under Section 23(r)(1). The Circuit Court of Appeals properly held that the latter section was not applicable.

Section 23(r)(1) of the Revenue Act of 1932 (c. 209, 47 Stat. 169) is a severely discriminatory provision, because it does not apply to non-capital assets other than stocks or bonds. It restricts deductions on "losses from sale or exchanges of stocks and bond * * * which are not capital assets * * * to the extent of the gains from such sales or exchanges". It appears that petitioner would contend that under this discriminatory provision, respondent, to deduct the loss suffered through the insolvency of the corporation in which he was a "preferred stockholder", should have gone into the market and gambled for gains on stocks and bonds to make sufficient profit to entitle him to a deduction. In other words, it interprets the above-quoted portion of Section 23(r)(1) to mean that receipt of a distribution on liquidation is exactly on equality under the law with a stock-market speculation. Such an interpretation is absurd.

With such a discriminatory provision and such an extended interpretation the Courts should seek the true intent, purpose and meaning of the statute before making a harsh and restricted interpretation. This was done by the minority of the Board of Tax Appeals in making their dissent and by the majority of the Court below by turning to the legislative history of the section in question.

(R., pp. 34, 36, 69.) Resort to legislative history frequently has been approved by this Court.

Helvering v. New York Trust Co., 292 U.S. 455, 464, 54 S. Ct. 806, 808.

The legislative history clearly discloses that Congress only intended to restrict deductions for losses on stocks and bonds from *actual* sales and exchanges. It so intended in order to eliminate a common method of tax avoidance by preventing owners of depreciated securities selling or exchanging the same at a loss and taking deductions on such losses against taxable gains from all other sources. Liquidation of corporations cannot be manipulated with sufficient ease to effect the tax evil which Congress sought to correct and, therefore, the statute should not be interpreted to go beyond the ordinary meaning of the words "sales and exchanges" used therein and the intent of Congress.

For brief legislative history see R., pp. 34-36;

Senate Report No. 665, 72nd Congress, 1st Session, p. 10;

H. R. Report No. 708, 72nd Congress, 1st Session, p. 12.

Section 23(r)(1) has come before the Courts in only one known and published instance and then only on a challenge of its constitutionality. In sustaining the constitutionality of the section, the Circuit Court of Appeals for the Seventh Circuit recognized the above-expressed legislative intent and held that the section was aimed only to prevent "speculative losses"—"losses from transactions which may often be but one form of gambling".

Davis v. United States, 87 Fed. (2d) 323, 325.

We respectfully submit that investment in a corporate enterprise, particularly in a corporation with few stockholders and unlisted issued stock, may not be interpreted as being "speculative" or a "form of gambling" as described in the legislative record or the above-cited Court decision. A loss sustained through the insolvency of a legitimate business corporation in the years of financial depression and the distribution of its assets, first, in full payment to its general creditors and, secondly, in insufficient payment to its next preferred creditors—its "preferred stockholders"—cannot be classified as a "gambling loss" or a "speculative loss" unless the Court believes that any person holding stock in any legitimate enterprise during a period of depression is, *per se*, a gambler and speculator.

In considering the above statement we ask the Court to appreciate the fact that, if the preferred stockholders had received nothing from the corporation, they would have been able to deduct the entire amount of their loss. This because the loss would not have resulted from a sale or exchange, but because the stock had become entirely worthless. This assertion has been accepted by the Government's representatives throughout the proceedings. The holders of the common stock, having received nothing on the liquidation, were permitted to deduct their full loss, although they suffered less financial loss than did respondent. We state this situation to emphasize the discriminatory character of Section 23(r)(1).

CONCLUSION.

The question of the meaning of Section 23(r)(1) of the Revenue Act of 1932 (c. 209, 47 Stat. 169) here presented, as far as we have been able to ascertain through diligent inquiry and research, has never arisen before or been presented to the Board of Tax Appeals or any Court, except in these proceedings. Petitioner has failed to present the existence or pendency of any parallel. As Section 23(r)(1) was repealed by the Revenue Act of 1934 (c. 277, 48 Stat. 680), the probability is that no parallel will arise or, if presented, will be barred by limitation. Therefore, petitioner may not claim privilege of a writ because the decision of the Court below considered some legal principles which might be associated with the issue in question.

United States v. Rhuer, 220 U.S. 547, 31 S. Ct. 596.

We respectfully submit that petitioner herein is not entitled to have writ of certiorari issue and that its petition should be denied.

Dated, San Francisco, California,
September 14, 1938.

ADOLPHUS E. GRAUPNER,
ARTHUR E. COOLEY,
Counsel for Respondent.

Due service and receipt of a copy of the within is hereby admitted

this _____ day of September, 1925.

_____

Solicitor General of the United States,
Counsel for Petitioner.

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In the Supreme Court
OF THE
United States

October Term, 1938

No. 304

Guy T. Helvering, Commissioner of Internal Revenue,
Petitioner,

vs.

Chester N. Weaver Company (a corporation),
Respondent.

BRIEF FOR RESPONDENT.

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San Francisco, California,
November 2, 1938.

TO THE HONORABLE JUSTICES
OF THE SUPREME COURT OF THE
UNITED STATES:

The printing of the attached brief was completed this day and forwarded immediately for timely filing with the Clerk of the Court as prescribed by paragraph 3 of Rule 27. This brief was prepared in reply to a typewritten proof of a brief received by us from the Solicitor General on October 24, 1938.

This day (after this brief was printed and one week after the time allowed by paragraph 1 of Rule 27 for petitioner to file its brief) we received a typewritten redraft of petitioner's proposed brief. The redraft materially changes the attitude and argument contained in the first proof and its accompanying letter intimates further possible changes.

In order to comply with the rules of this Court, we will be unable to rewrite and print a brief replying to petitioner's tardy amended brief or to await further changes and file the same within the time allowed by the Rule 27. Therefore, this brief is respectfully submitted as reply to petitioner's original argument.

ADOLPHUS E. GRAUPNER,
ARTHUR E. COOLEY,
Counsel for Petitioner.

In the Supreme Court
OF THE
United States

October Term, 1938

No. 304

Guy T. Helvering, Commissioner of Internal Revenue,
Petitioner,

vs.

Chester N. Weaver Company (a corporation),
Respondent.

BRIEF FOR RESPONDENT.

I. INTRODUCTORY STATEMENT.

Petitioner's brief contains certain statements which are erroneous or faulty in conclusion. To these we first refer, in order that the Court may more readily appreciate respondent's position.

1. Petitioner seeks to involve section 101 of the Revenue Act of 1932 (c. 209, 47 Stat. 169) and the cases of *White v. United States*, Nos. 96 and 97 on the present calendar in this case. Section 101 relates to capital gains and losses, which are not herein involved, and by its

expressed terms is not applicable to corporations, *White v. United States* does not involve section 23(r)(d) of the 1932 Act, upon which petitioner rests its case.

2. Petitioner assigns its errors to make it appear that the deduction approved by the Court below had been allowed on severance of the statute involved rather than considering the applicable provisions as a whole. The decision of the Court below discloses that it considered all other provisions of the Revenue Act of 1932 relating to deductions, including section 23(r)(1).

3. Also, in the opening statement of its argument petitioner erroneously assumes that respondent has not "pointed to an applicable statute" under which it is entitled to a deduction.

Respondent, throughout the progress of this case, has called attention to specific statutory provisions which entitle it to the deduction sought and the Court below gave careful attention to each of the statutory provisions to which its attention was called, viz: Sections 22(d), 115(c), 111 and 112 of the Revenue Act of 1932 (c. 209, 47 Stat. 169). These are specific statutes relating to a particular matter, whereas section 23 is a general statute covering deductions generally.

However, as we have constantly asserted, if this complete specific statutory procedure relating to distributions by corporations did not exist, the only part of the general statute that could possibly apply here would be section 23(f) and not section 23(r)(1), because the latter applies only to "sales or exchanges", and a distribution *required by law* on dissolution of a corporation is neither a sale or exchange.

II. SUMMARY OF ARGUMENT.

1. The position of petitioner that the loss herein involved is not deductible under section 23(r)(1) of the Revenue Act of 1932 (c. 209, 47 Stat. 169, Appendix p. ii) requires it to establish that the words "sales or exchanges" as used in said section have a meaning extended beyond the ordinary definition of those words. If there was no "sale" or "exchange" then petitioner must fail.

2. Under section 22(d), 115(c), 111 and 112 respondent is entitled to deduction of its loss, without reference to any other sections of the Revenue Act of 1932.

3. Further, under sections 22(d), 115(c), 111 and 112 of the same Act (Appendix pp. i, ii, iii) respondent is entitled to deduct the loss sustained under section 23(f), despite the provisions of section 23(r)(1).

4. Petitioner's arguments on other points are inadequate to sustain its position in seeking to deprive respondent of right to deduction.

III. ARGUMENT.

The order of argument contained in petitioner's brief herein is altered for what we believe to be a more logical analysis of the petitioner's attack upon the decision of the Court below:

1. THE LOSS CANNOT BE DENIED BECAUSE OF ANY APPLICABILITY OF SECTION 23(r)(1).

Because the majority of the Court below considered that section 23(r)(1) was not applicable to limit the de-

duction sought by respondent and because the minority relied upon the same section to sustain its dissent we believe that section should be first discussed.

Throughout the progress of this case from the Bureau of Internal Revenue to this Court the government has conceded that the amount involved herein would have been deductible under section 23(f), if it were not for what it asserts to be a controlling limitation in section 23(r)(1). Section 23(f) provides that in computing net income there shall be allowed as a deduction:

> "(f) Subject to the limitations provided in subsection (r) of this section, in the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise."

The whole of subsection 23(r) is not involved. That portion upon which petitioner relies reads as follows:

> "(r) **Limitation on Stock Losses**—(1) Losses from *sales or exchanges* of stocks and bonds * * * which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of its own obligations)." (Italics supplied.)

There is no controversy over the character of the assets involved in the transaction before the Court. It is conceded that they were not capital assets.

The majority opinion holds that section 23(r)(1) is not applicable to limit deductions for losses sustained on the distribution of the remaining assets in complete liquidation of an insolvent corporation (R. p. 69), while the minority opinion holds to the contrary. (R. p. 71.)

Petitioner lays great stress on the dissent to the decision of the Court below. The premise of fact in that dissent is that the "holders of all the preferred stock of the Townsend Company, surrendered their stock certificates for cancellation and for the purpose of completing liquidation and effecting the dissolution of that company." (R. 71.)

From that premise, Judge Stephens reaches the conclusion that the transaction was a sale or exchange within the meaning of section 23(r)(1). The statement of fact is correct, but the facts on which he relies destroy the effectiveness of the conclusion he reaches.

Considering all of the sections heretofore and hereinafter discussed, the minority judge rejects the applicability of all, excepting sections 23(f) and 23(r)(1), and applying those subsections in conjunction with sections 11, 12, 13 and 21 of the Revenue Act of 1932, reaches a conclusion which is based on the following facts (R. 71):

1. The Townsend Company became financially involved and unable to continue business;

2. The stockholders took the necessary steps to dissolve and liquidate;

3. The assets of the company were sold for $26,780.50;

4. The holders of all the preferred stock surrendered their certificates for cancellation in order:

(a) to complete liquidation of the company, and

(b) to effect dissolution of that company;

5. The $26,780.50 received for the assets was distributed to the preferred stockholders pro rata, and

6. Respondent herein received $13,140.25, for the $100,000 it had invested.

7. Also, it is to be supposed that he considered that the preferred stock owned by respondent was non-voting stock, subject to redemption at a fixed price at any time by the corporation, and, on dissolution, subject to preference over common stock on distribution of assets: (R. 49, 50.) These factors placed respondent on but little different basis than if it had been a bondholder.

Applying these facts to the term "sales or exchanges of stock and bonds" as used in section 23(r)(1), there is not a single element which would bring the transaction within the intendment of section 23(r)(1). The minority judge has in effect reached his conclusion by judicial legislation rather than by judicial interpretation.

Section 23(r)(1) uses the simple words "sales or exchanges" for the purpose of limiting the deduction of losses. The concept of "sales and exchanges" is so different from the transaction herein involved that merely to state the proposition is to prove it. Ordinary words, ordinarily used, must be interpreted in their ordinary sense.

The word "sale" in its ordinary sense means a transfer of property for a fixed price in money or its equivalent.

United States v. Benedict (C.C.A. 2), 280 Fed. 76, 80.

A "sale" *is a contract* whereby one acquires property in the article sold and the other parts with it for a valuable consideration.

Vol. 4 *Words and Phrases* (2nd Series) 437;
California Civil Code, Section 1721(2).

"Sale" is not a vague or uncertain word, it is a word of precise legal import, both at law and in equity.

Williamson v. Berry, 8 How. 495, 544, 49 L. Ed. 492, 543.

The word "exchange" is generally regarded as synonymous with "barter", "swap", or "trade"—an exchange of one article for another.

"A 'sale' means for money. An 'exchange of property' is a mere barter or trade."

Ewers v. Weaver, 182 Fed. 713, affirmed (C.C.A. 8), 195 Fed. 249;
Spalding v. C. I. R., 7 B.T.A. 588, 590.

The general and common description of a complete liquidation of a corporation is well expressed by the California statute applicable thereto:

"After determining that all the known debts and liabilities of a corporation in the process of winding up have been paid or adequately provided for, *the directors shall distribute* all the remaining corporate assets among the shareholders according to their respective rights and preferences." (Italics supplied.)
Civil Code, section 401(a).

Following the foregoing legal requirement, the Townsend Company was liquidated. All the elements of a sale or exchange were missing:

(a) The shareholders, like respondent herein, had no election but to accept the distribution;

(b) The directors of the corporation faced a legal duty, from which all contractual elements were missing;

(c) There was no adequacy of consideration, because there was no value to the corporation in the stock which was surrendered to it for liquidation;

(d) The shareholders were not required to give anything in return for the assets distributed, because there was no statutory or contractual requirement that they surrender their stock. The stock could be cancelled on the corporation's books without surrender of the certificates for shares. If surrendered, the certificates would have no value to the corporation;

(e) There was no open market for sale or exchange of either the stock or the assets—the law required the assets to be distributed to the shareholders, something not in the nature of a sale or an exchange.

See: *C. M. Mensies, Inc., v. C. I. R.*, 34 B.T.A. 163, 168.

Comparing the foregoing legal aspects of a distribution in liquidation of a corporation with the factual elements used as a premise by Judge Stephens for his minority decisions (supra), it is clear that his conclusions are unsound both in fact and in law.

No "sales or exchanges of stocks and bonds" require any accounting entries on the part of a corporation, other than entries in the stock transfer ledger. However, when we come to consider the accounting of the corporation in

relation to its status with its stockholders we find a normal situation which precludes the application of any theory of "sales or exchanges". On the books of the corporation we find paid in capital as an asset and outstanding shares of stock as a liability. A situation not comparable with that of vendor and vendee. As long as the stock is outstanding, no matter how often the shares may change possession on "sales or exchanges" and regardless of the value of the consideration paid for stock on "sales or exchanges", the corporation's liability on that outstanding stock remains static. Only when it redeems the stock does the situation change—paid in capital and liability on the outstanding stock are both reduced. The whole transaction is something apart from the stockholder, except that when it comes to a redemption of his stock, whether for more or less than his subscription price, he is compelled to accept what the corporation pays him and the corporate liability is written off on its books. If the redemption of such stock is made in complete liquidation the books of account will not indicate a sale, but the satisfaction of a liability, and cross entries will be made to close the books. While the corporation will remain in possession of the surrendered shares on its liquidation, nevertheless those shares will have no value represented in the closed accounts.

There is a strong parallel between the redemption of shares of preferred stock and bonds issued by a corporation. Both have preferences over subordinate issues and both are subject to the call of the corporation regardless of any desire of the holder to present them for redemption. Yet, the government has consistently claimed that

the redemption of bonds is not a sale or exchange and the courts and the Board of Tax Appeals have sustained that claim.

United States v. Fairbanks, 95 Fed. (2d) 794, 796, Cert. denied by this Court October 10, 1938;

Cook v. Commissioner, 38 B.T.A., No. 87, decided Sept. 29, 1938.

If redemption of bonds is not a "sale or exchange", then redemption of preferred stock should have the same exclusion.

Legislative history was cited by both parties before the Court below and the Board and was considered by both tribunals. Petitioner now asserts that the statute is unambiguous and resort to legislative history is not necessary. After considering the differences of opinion in the decision of the Court below and reading the involvement of sections of the statute which are found in petitioner's brief, the assertion obviously is incorrect. In appendix "B" hereto (pp. iv-vi) we recite the legislative history presented by the respondent herein to the Circuit Court of Appeals. We but summarize the intent of section 23(r)(1) as indicated by the Ways and Means Committee of the House and the Finance Committee of the Senate to show that "distributions by corporations" were never considered by any of the committees as the object at which the section was aimed.

This Court has consistently held that it should turn to legislative history to determine the meaning of doubtful statutes.

Wright v. Mountain Trust Bank, 300 U.S. 440, 463, 464;

Helvering v. New York Trust Co., 292 U.S. 455, 464; *United States v. Katz*, 271 U.S. 354, 357.

Because petitioner has sought an interpretation of section 23(r)(1) far beyond the expressed intent of and the language used by Congress, we point to the legislative history.

In 1932 Congress was confronted with the fact that many taxpayers were avoiding all income tax by selling securities at a loss "in the stock and bond markets" in sufficient amounts to eliminate their gains from all other sources. (Appendix, pp. iv-vi.) The Ways and Means Committee and the Finance Committee were of the opinion that "*some limitation*", not a general limitation, should be placed on permitting the allowance of "*such losses.*" (Appendix, p. iv.) The Treasury Department were in accord with "some limitation" being placed on "the deduction of losses" from the "*sale*" of securities. (Appendix, p. iv.) This limitation always referred to "stock and bond market transactions", "security transactions", "manipulation so as to create fictitious losses", "preventing speculative losses", etc. (Appendix, pp. iv-vi.)

It thus is evident that Congress aimed to limit something far different from "distributions by corporations" and particularly distributions in "complete liquidation of a corporation." It did not contemplate a broad limitation, it sought only to restrict those transactions commonly employed for tax avoidance. Obviously the liquidations of corporations at a loss were too infrequent, too awkward to manipulate, and subject to too many delays to accom-

plish the tax evil upon which Congress sought to place "some limitation".

Petitioner relies entirely upon the contention that the distribution of the liquidating dividend involved in this transaction was such a sale or exchange as came within the limiting provisions of section 23(r)(1). In other words it seeks to enlarge the meaning of the words "sales or exchanges" beyond their common meaning.

Section 23(r) began and closed its existence with the Revenue Act of 1932 (c. 209, 47 Stat. 169), it was a restricted and shortlived special statute. Such a special statute, which did not specifically amend or include by reference other special statutory provisions, can receive only the most restricted interpretation by the Court.

United States v. Barnes, 222 U.S. 513, 519.

Section 23(r)(1), because it limits deductions for losses only to "sales or exchanges of stocks and bonds" without in any way indicating any intent or purpose to enlarge the ordinary meaning of the words "sales or exchanges", must be considered by the Court strictly in the light of the language used in the statute. If there was no sale or exchange within the common meaning of the statutory language, then the question as to whether there was a loss in some other manner has no significance. Congress must be presumed to have used words in their ordinary meaning.

Old Colony R. Co. v. Commissioner, 284 U.S. 552, 560, and cases there cited;

United States v. Kirby Lumber Co., 284 U.S. 1, 3.

Petitioner seeks to distort section 115(c) by interpreting the phrase "shall be *treated* as in part or full payment in exchange for the stock", for *determination* of gain or loss upon the complete liquidation of a corporation under section 111 and recognition under section 112(a), to mean an actual sale or exchange, such as section 23(r)(1) contemplates. The courts should avoid refined or strained analogies such as petitioner seeks to draw in interpreting revenue statutes.

Woolford Realty Co. v. Rose, 286 U.S. 319, 329;
Welsh v. Commissioner, 63 Fed. (2d) 976, aff'd 290 U.S. 111.

When subsection 23(r)(1) was enacted to mitigate a specifically described tax abuse and referred only to "sales or exchanges", without specific limitation on or inclusion of any other transaction, the specific transactions described—"sales or exchanges"—are beyond enlargement by any court. The maxim "*expressio unius est exclusio alterius*" is clearly applicable.

> "'When a statute limits a thing to be done in a particular mode, it includes the negative of any other mode' (*Botany Mills v. U. S.*, 278 U.S. 282, 289, 73 L. Ed. 379)."

Paso Robles M. Co. v. Commissioner, 33 Fed. (2d) 653, 654, Cert. den'd. 280 U.S. 595.

What petitioner has been asking for and what the Court below denied falls within the following prohibition:

> "What the government asks is not the construction of a statute, but, in effect, an enlargement of it by the court, so that what was omitted, presumably by

inadvertence, may be included within its scope. To supply omissions transcends the judicial function."

Iselin v. United States, 270 U.S. 245, 251.

The courts may not "graft" something on a statute which is not there.

Smietanka v. First T. & S. Bank, 257 U.S. 602, 606.

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2. UNDER SECTIONS 22(d), 115(c), 111 AND 112 RESPONDENT IS ENTITLED TO DEDUCTION OF ITS LOSS WITHOUT LIMITATION OF ANY OTHER SECTIONS OF THE REVENUE ACT OF 1932.

Petitioner's second specification of alleged error in the decision is that a loss resulting from a corporate liquidation is deductible under the provisions of Sections 22(d), 115(c), and 112 of the Act (The decision, of course, considered Section 111).

Supplement B of subtitle C has legislative entitlement in the index and in the body of the official 1932 Act, viz: "**Computation of Net Income**". Under this heading is Section 115, entitled "**Distributions by Corporations.**"

Section 13, entitled "**Tax on Corporations**", provides that a tax of 13¾% shall be paid "upon the *net income.*"

Section 22(d), entitled "**Distributions by Corporations**", provides: "Distributions by corporations shall be taxable to the shareholders *as provided in section 115.*"

There are *two* parts of the Act devoted to and legislatively entitled "Computation of Net Income"—the first comprising sections 21-26, inclusive, and the second com-

prising sections 111-120, inclusive. The latter part contains the *specific* provisions for handling the *computation* of *net* income where "distributions by corporations" are involved and provides a complete procedure therefor.

There being, then, a complete *specific* procedure for the treatment of distributions in liquidation of a dissolved corporation, such specific statutes, under the universally accepted rule of statutory construction, must prevail over the *general* provisions of section 23.

Kepner v. United States, 195 U.S. 100, 125;
Missouri v. Ross, 299 U.S. 72, 86;
Murphy Oil Co. v. Burnet, 55 Fed. (2d) 17, 25.

Petitioner contends that "the sections relied upon by the majority below do not permit deduction of a loss", but such contention annuls the mandate of 115(c) that "the gain or loss to the distributee * * * *shall* be determined under section 111, but *shall* be *recognized* only to the extent provided in section 112."

Petitioner then argues that *recognizing* a loss does not determine its deductibility. *If that were so, then there never could be any deduction under the act for the* GENERAL *section, 23, says "there shall be* ALLOWED *as deductions"—and "allow" is synonymous with "recognize."*

Webster's New International Dictionary gives the following as synonyms of "recognize": "Own, admit, *allow*, avow, confess."

The fact that the word "recognized" rather than "allowed" was used in 115(c) is of no significance.

"It has, indeed been said that generally, statutes in pari materia ought to receive a uniform construction,

notwithstanding any slight variations of phrase; the object and intention being the same."

Endlich, "Interpretation of Statutes", Sec. 381.

That the object and intention were the same is evident from the fact that both the general and special subdivisions are entitled, within the Act, "Computation of Net Income."

As was approved in *Lynch v. Alworth-Stephens Co.*, 267 U.S. 364 at 370, "the plain, obvious, and rational meaning of a statute is always to be preferred to any curious, narrow, hidden sense that nothing but the exigency of a hard case and the ingenuity and study of an acute and powerful intellect would discover."

The plain, obvious and rational meaning of the word "recognized" is that the loss must be allowed in "computing the net income", under which heading these sections occur.

Since it is made mandatory that the loss be recognized or allowed as provided in the *specific* statutes, it is not necessary to apply the provisions of the *general* section (23). The Court will not consider that this mandate in the specific statute was an idle gesture by the Congress. The only way a loss can be recognized or allowed is to deduct it from gross income and any other view destroys the obvious intent of section 115(c).

It is the duty of a court in the construction of a statute, to avoid absurdities and to give effect to the evident object and purpose of a legislative act, and the title of the section may be considered for that purpose.

Church of the Holy Trinity v. United States, 143 U.S. 457, 36 L. ed. 226, 228-9.

The title of Supplement B, "Computation of Net Income", makes doubly clear the meaning of the word "recognized" as used in Sections 111, 112 and 115.

The procedure of 115(c) being complete for the purpose of computing the net income (upon which under Section 13 the tax is to be paid), and the mandatory language of 115(c) designating the particular sections to be applied, such mandate necessarily excludes consideration of sections 101 and 23(r)(1), under the maxim "*expressio unius est exclusio alterius.*"

> "When a statute limits a thing to be done in a particular mode, it includes the negative of any other mode."
>
> *Botany Worsted Mills v. United States*, 278 U.S. 282 at 289.

Counsel seek to inject section 101 into the discussion, but that section *specifically* [subdivisions (a) and (b)], *excludes corporations,* and, furthermore, it is not referred to in section 115(c)—which provides the complete procedure for the handling of distributions in liquidation of a corporation. Section 101 is not one of the sections included under the heading of "Supplement B—Computation of Net Income." Section 101, like 23(r)(1), not being mentioned in section 115(c), comes also within the maxim, "expressio unius est exclusio alterius."

Petitioner states that "such a limitation of section 115(c) *leaves the capital gain and loss provisions of the statute inapplicable.* Section 101(a) infra, permits taxation of gains from the sale or exchange of capital assets at a 12½% rate." (Italics supplied.)

We entirely agree that section 115(c), by its explicit and mandatory wording, excludes consideration not only of 23(r)(1) but also of 101(a). It is clear from the language of 115(c) that the Congress did not consider that a distribution in liquidation was a sale or exchange, either of capital or non-capital assets, and purposely eliminated any possible application of the general capital gain and loss provisions. *If they had not so intended there would have been no purpose in enacting 115(c).* Absent 115(c), the matter would have been included in the general statutory provisions governing losses.

Article 625 of Regulations 77 (administrative provisions for the 1932 Act) provides:

> "The gain or loss to a shareholder from a distribution in liquidation is to be determined, as provided in section 111 and article 561, by comparing the amount of the distribution with the cost or other basis of the stock provided in section 113 and articles 591-606; but the gain or loss will be recognized only to the extent provided in section 112 and articles 571-581."

The Court will note that, even in the Treasury Department's interpretation, there is no suggestion of any limitation by section 23(r)(1) or that 101(a) is to be applied to a loss resulting from a corporate dissolution and distribution. The present theory of petitioner is an afterthought—not supported by the Act, the department regulations, or the intent of the Congress.

When we come to carefully consider section 111, to which section 115 specifically refers, and its reference to section 112, we find the following:

(a) Section 111, immediately follows the statutory heading of Supplemental B, entitled **"Computation of Net Income"**, something that cannot be done without deductions of losses from gains.

(b) Section 111 is given the statutory entitlement —**"Determination of amount of gain or loss"**. "Determination means decisive action."

(c) Subsection (a) is entitled **"Computation of gain or loss"**. Computation means the calculation of the results of a transaction to determine whether there is profit or loss.

(d) Subsection (c) is entitled **"Recognition of gain or loss"** and loss may have no recognition under the revenue laws unless it is deductible. The subsection then refers to section 112 for the *determination* of the gain or loss recognizable under section 111.

(e) Section 112(a) provides that *"the entire amount of the* gain or *loss, determined* under section 111, *shall be recognized."*

The foregoing brief analysis should effectively refute the arguments of petitioner and sustain the decision of the Court below.

---

3. RESPONDENT IS ENTITLED TO DEDUCTION OF ITS LOSS UNDER SECTION 23(f) BECAUSE OF THE CONTROLLING EFFECT OF SECTIONS 22(d), 115(c), 111 AND 112a.

Petitioner further argues that the loss sustained by respondent is not deductible under section 23. Of course

this argument is based solely on the unsound contention that section 23(f) is so limited by section 23(r)(1) that no deduction may be granted to respondent. Evidently this argument is based upon a statement found in the minority opinion of the Court below, viz.:

> "If losses on liquidation distributions are to be governed by the provisions of section 22(d), 115(c), 111 and 112 without regard to section 23, logic would lead to the conclusion that section 23(r) is in no case to be given effect." (R. p. 74.)

The minority opinion thus ignores the facts, the law, reason and logic; it ignores the breadth of section 23(f) and the narrowness of section 23(r)(1).

As was said in *Baltimore & O. R. Co. v. Western Union Tel. Co.*, 242 Fed. 914, 915, "the right to exchange implies the right to fix the rate, method, or amount of exchange."

In a corporate dissolution, law, not bargaining, fixes what the stockholder shall receive. He has no power to fix the rate, method or amount of exchange. He cannot say how many shares he will surrender nor how much shall be distributed to him. He is not a free agent bargaining with a prospective purchaser. He takes what the law distributes to him.

18 *C. J.* 1291-2 defines "distribution":

> "The act of distributing or dispensing; the act of dividing or portioning among several or many; the act of dividing or making an apportionment; apportionment."

There is no process of "bartering", "swapping" or "trading" between the parties in such a situation; there

is nothing as to price or consideration upon which they must "mutually agree"—for the law fixes just what must be done.

> "Of course, on dissolution of the Finance Company, the title to its property passed to the persons who were its stockholders at the time of the dissolution."
>
> *North Hollywood M. Co. v. North American B., etc., Co.*, 137 Cal. App. 180 at 186.

Section 23(r)(1) by its express terms limits the other subsections of section 23 only as to "losses from sales or exchanges of stocks and bonds." On all other losses sustained by a corporation "during the taxable year and not compensated for by insurance or otherwise", it is entitled to a deduction under section 23(f) by law, reason and logic.

Respondent believes that even if sections 22(d), 115(c), 111, and 112 were in themselves inadequate to permit the deduction, nevertheless the sections define "distributions by corporations" in such a way and fix such a method of computation, determination and recognition of losses thereunder that, under the facts in this case and in accordance with reason and logic, section 23(f) would permit the deduction without possibility of effect from the specific limitation found in section 23(r)(1).

Section 23(r)(1) being a limitation on specific transactions and permitting only specific offsets cannot, as we have argued at length in paragraph 1 of our argument, effect a limitation on other transactions. Note that section 23(r)(1) allows deductions of "losses from sales or exchanges of stocks and bonds" * * * "only to the extent

of the gains from such sales or exchanges." It is difficult to see how gains from "sales or exchanges of stocks and bonds" could, under the wording of the statute and in accord with logic, be offset against losses from the complete liquidation of a corporation. It is more difficult to conceive of the Commissioner of Internal Revenue agreeing to the proposal that the two were akin and that a gain from the liquidation of a corporation might be offset against a loss from a sale of stock. Credulence *in extenso* cannot conceive of the Commissioner conceding such a claim and he would at once submit to section 23(f) rather than permit the injection of what, under such an example, he would claim to be forbidden tax avoidance.

---

4. SUPPLEMENTARY REPLY TO PETITIONER'S BRIEF.

Petitioner, by taking segments from the decision of the Court below, seeks to discredit the prevailing decision. The gist of that decision is that "by its terms section 23(r)(1) applies only to 'sales or exchanges'," and that "the liquidating dividend here is neither within the ordinary and accepted meaning of those terms." This conclusion is sound and petitioner has in no way overcome it. What petitioner seeks is to have this Court legislate to extend the meaning of the words "sales or exchanges" and that is beyond the Court's powers.

Heiner v. Donnan, 285 U.S. 312, 331.

Petitioner expends considerable space in arguing as to the capital gain and loss provisions of the Revenue Act of 1932. No capital gain or loss is involved in this matter.

Moreover, the provisions of section 101 relating to capital gains or losses have no application to a corporation, such as petitioner herein contends. Petitioner thus seeks to confuse the argument in this case or seeks to inject the issues in the cases of *White v. United States* (Nos. 96 and 97 of this calendar) where they do not belong. In either event its endeavors are erroneous.

Petitioner seeks to belittle the exemplar stated in the opinion of the Court below (R. p. 70) to show the absurdity of the statutory interpretation sought by it. Only by comparisons may absurdities be shown, and the Court below but followed the precedents of years standing.

Petitioner contends that the "recognition" of a loss under section 112 is not in any sense a determination that the loss is deductible, and argues that, if recognition of a loss under that section permitted deductions, subsections (f) and (r), and other subsections of section 23 which are not here at issue, were needless enactments. In reply we would point out that had Congress not intended to discriminate between various transactions so that some would be taxable, some not subject to tax, some subject to deductions and some not subject to deductions, sections such as 22(d), 22(e), 101, 111, 112, 113, 114, 115 and 116 would never have been enacted.

When it enacted sections 22(d) and 115 giving distributions by corporations a separate taxable status, Congress could not have intended that the recognition of gain or loss could be disturbed by sections of restricted meaning and limited application, such as section 23(r)(1), unless that section contained language to make it applicable or

unless section 115 was amended to show that Congress intended to enlarge the meaning of "distributions in liquidation", so that they fell within the definition of "sales or exchanges", where they do not properly belong in common or legal usage.

IV. CONCLUSION.

It is respectfully submitted that the decision of the United States Circuit Court of Appeals for the Ninth Circuit should be affirmed.

Dated, San Francisco, California,
November 2, 1938.

ADOLPHUS E. GRAUPNER,
ARTHUR E. COOLEY,
Counsel for Respondent.

(Appendicies A and B Follow)

Appendix A

REVENUE ACT OF 1932, c. 209, 47 STAT. 169:

SEC. 21. NET INCOME.

"Net income" means the gross income computed under section 22, less the deductions allowed by section 23.

SEC. 22. GROSS INCOME.

(a) **General Definition.**—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * * *

(d) **Distributions by Corporations.**—Distributions by corporations shall be taxable to the shareholders as provided in section 115.

(e) **Determination of Gain or Loss.**—In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in sections 111, 112, and 113.

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * * *

(e) **Losses by Individuals.**—Subject to the limitations provided in subsection (r) of this section, in the case of

an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—

(1) if incurred in trade or business; or

(2) if incurred in any transaction entered into for profit, though not connected with the trade or business;

* * * * * * *

(f) **Losses by Corporations.**—Subject to the limitations provided in subsection (r) of this section, in the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.

* * * * * * *

(r) **Limitation on Stock Losses.**—(1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges (including gains which may be derived by a taxpayer from the retirement of his own obligations).

* * * * * * *

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) **Computation of Gain or Loss.**—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113(b), and the loss shall be the excess of such basis over the amount realized.

(b) **Amount Realized.**—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

(c) **Recognition of Gain or Loss.**—In the case of a sale or exchange, the extent to which the gain or loss determined under the section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

(d) **Installment Sales.**—Nothing in this section shall be construed to prevent (in the case of property sold under contract providing for payment in installments) the taxation of that portion of any installment payment representing gain or profit in the year in which such payment is received.

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) **General Rule.**—Upon the sale or exchange of property the entire amount of the gain or loss determined under section 111, shall be recognized, except as hereinafter provided in this section. * * *

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

(c) **Distributions in Liquidation.**—Amount distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. * * *

Appendix B

LEGISLATIVE HISTORY OF SUBSECTION 23(r).

On the revision of the Revenue Act of 1928, C. 852, 45 Stat. 791, by the Revenue Bill of 1932 (H.R. 10,236) the Ways and Means Committee of the House of Representatives proposed five additional and related subsections to Section 23, viz.: (r), (s), (t), (u) and (v), and in so doing stated (H.R. Report No. 708, 72nd Congress, 1st Session, p. 12):

> "Many Taxpayers have been completely *eliminating* from tax their income from salaries, dividends, rents, etc., by deducting therefrom *losses sustained in the stock and bond markets,* with serious effect upon the revenue. Your Committee is of the opinion that *some limitation ought to be placed on the allowance of such losses.*" (Italics supplied.)
>
> • • • • • • •

Note that the committee states "some limitation" was deemed advisable—a clear indication of narrow, rather than broad, limitation. The proposed amendments were aimed at "losses sustained in the stock and bond markets" (supra) and intended to apply to trading losses for, after explaining the reason for excluding "dealers in securities" from the limitations, the Report proceeds to state (p. 13):

> "Traders or other taxpayers *who buy and sell securities for investment and speculation,* whether or not on their own account, and irrespective of whether such *buying or selling* constitutes the carrying on of the trade or business, are not regarded as dealers in securities within the meaning of this rule." (Italics supplied.)
>
> • • • • • • •

After H.R. 10,236, passed the House and was sent to the Senate, the Finance Committee held hearings on the bill and called the then Secretary of the Treasury as a witness. In regard to the proposed addition of subsections 23(r), (s), (t), (u) and (v), the Secretary of the Treasury made explanation to the Committee (Hearings Before the Committee on Finance, United States Senate, Seventy-Second Congress, First Session, on H.R. 10,236, p. 31) as follows:

"In recent years income from business profits, from salaries, and from other sources, has in many cases been offset by losses on *security transactions. It is the effect of such losses* in diminishing the tax upon forms of income, such as I have mentioned, which, to a considerable extent, is responsible for the diminished yield of the income tax in these years."

* * * * * * *

"In other words, people have been able through the taking of *losses on sales of securities* to wipe out any profits by way of dividends, or from business, and so forth. And in some cases *the selling of securities and the taking of losses* have not represented actual losses, but nevertheless they have been enormously effective in wiping out what we have described as other income."

* * * * * * *

"Now, *the Ways and Means Committee felt, and the Treasury agreed,* that the abuse has grown to such a point that something ought to be done about it. * * * So the Treasury did agree with the Ways and Means Committee that you ought to *limit the deduction of losses from the sale of securities,* and that *the loss resulting from sale* of securities should not

be used to wipe out other income." (Italics all supplied.)

* * * * * * *

The Senate Finance Committee amended H.R. 10,236 by reducing the five proposed additions to Section 23 to three, viz.: (r), (s) and (t). In reporting the bill to the Senate, the Committee stated (Senate Report No. 665, 72nd Congress, 1st Session, p. 10):

"The House bill adopted very severe limitations upon the allowance of losses *from the sale of securities,* as a deduction in computing net income. The provisions were based on a twofold policy: (1) Protecting the revenues from the growing practice of reducing tax liabilities by the *sale of securities* on which losses had accrued, and (2) *preventing speculative losses* from wiping out ordinary income, which represents real tax-paying ability." (Italics supplied.)

* * * * * * *

Further in the report (p. 17), the Finance Committee stated, in confirming the Ways and Means Committee explanation of the object sought by amending Section 23 (H.R. Report No. 708, p. 12, supra), as follows:

"Many taxpayers have been completely or partially eliminating from tax their income from salaries, dividends, rents, etc., by deducting therefrom *losses sustained in the stock and bond markets,* with serious effect upon the revenue." (Italics supplied.)

Due service and receipt of a copy of the within is hereby admitted

this _____ day of November, 1938.

_____

Solicitor General of the United States

Counsel for Petitioner.

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1935

No. 304

RESPONDENT'S SUPPLEMENTARY BRIEF

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In the Supreme Court
OF THE
United States

October Term, 1938

No. 304

Guy T. Helvering, Commissioner of Internal Revenue,

Petitioner,

vs.

Chester N. Weaver Company (a corporation),

Respondent.

RESPONDENT'S SUPPLEMENTARY BRIEF.

PRELIMINARY STATEMENT.

Petitioner having failed to file its brief and serve the same on respondent's counsel within the time prescribed in paragraph 1 of Rule 27 of this Court and before the time necessary for respondent to forward its brief to the clerk of the above-entitled Court for filing within the time allowed by paragraph 3 of said Rule 27, this supplementary brief is presented.

The purpose of this supplementary brief is to reply to the contentions made by petitioner in its brief which was not received by respondent until November 5, 1938.

REPLY TO ARGUMENT.

In its preliminary draft of brief, received by respondent October 24, 1938, petitioner assumed the position that the statute under consideration is not ambiguous and resort to legislative history is unnecessary. Petitioner has now assumed a different attitude and has resorted to legislative history to support its position. This shift of attitude and its other changes of position require reply to those issues not presented or otherwise presented in petitioner's first preliminary draft.

---

1. SECTION 23(r)(1) DOES NOT CONTROL SECTION 115(c) TO PREVENT THE DEDUCTION SOUGHT.

Petitioner asserts that, because section 115(c) provides that "amounts distributed in complete liquidation of a corporation shall be *treated as* in full payment *in exchange* for the stock" and, because, the distribution to respondent herein was in cash, therefore, there was a sale of the stock. By linguistic juggling it transfers "exchange" into "sale", and then claims that there was a "sale or exchange" within the contemplation of section 23(r)(1). To support this act of legerdemain, petitioner cites two cases interpreting the Revenue Act of 1918 (40 Stat. 1057, c. 18) and legislative history referring to the Revenue Act 1924 (43 Stat. 253, c. 234), both of which statutes were

long ago repealed and revised when the Revenue Act of 1932 (47 Stat. 169, c. 209) was adopted.

See:

Federal Income and Estate Tax Laws (Fifth Ed.), by Barton and Browning, showing comparison of sections of Revenue Acts of 1918 to 1932 inclusive.

Section 201(c)(2) of the Revenue Act of 1918 (40 Stat. 1057, c. 18), which the cases of *Hellmich v. Hellman*, 276 U. S. 233 and *Landstaff v. Lucas*, 9 Fed. (2d) 691, cited by petitioner, apply to a statute which was repealed by the Revenue Act of 1921. (42 Stat. 227, c. 136.)

The two cases cited above distinguish between "dividends" and "distributions" as described in section 201(a) and (c) of the Revenue Act of 1918. They make no reference to any other section of that Act and no duty was imposed on the Courts in those cases to define the words "sales or exchanges" or to use carefully refined language to describe the distinctions involved, nor did the Courts attempt to do so. Therefore, the decisions are not apt or applicable to the conflicts between the other portions of the 1918 Act, or to any subsequent Act. Moreover, the Revenue Act of 1918 did not contain the conflicting provisions which are to be found in the Revenue Act of 1932. In no way can the decision of this Court in *Moore Ice Cream Co. v. Rose*, 289 U. S. 373, 377, cited by petitioner, be applicable as law in this case.

The Revenue Act of 1921 repealed section 201(c) of the 1918 Act and contained no similar provision. In the 1924 Act a section numbered 201(c), but differing in language from section 201(c) of the 1918 Act, was enacted.

With reference to section 201(c) of the 1924 Act, petitioner cites a portion of the legislative history to support its contention (Brief, p. 11)—carefully omitting any reference to the legislative history of the 1928 Act which entirely changed the arrangement and application of the Revenue Act of 1926 (44 Stat. 2, c. 27) which repealed but followed the form of the 1924 Act. In considering the Revenue Act of 1932, the Act of 1928 is of great import.

The Revenue Act of 1926 created a "Joint Committee of the House and Senate on Internal Revenue Taxation" and charged it with the duty of preparing a bill for the simplification of taxes, particularly the income tax.

Revenue Act of 1926 (44 Stat. 2, c. 27), section 1203(a). The result of the work of this Committee was H. R. 1, 70th Congress, known as The Revenue Bill of 1928. In presenting this bill, the Ways and Means Committee of the House stated (Report 2, 70th Congress, 1st Session, pp. 11, 12):

> "The Committee is impressed with the importance of making *a fresh start.* • • •
>
> "Therefore, the provisions of the income tax title of the present bill apply *only to the taxable year 1927 and succeeding years* and have no effect whatsoever on taxes imposed for *prior taxable years.*" (Italics supplied.)

Following the above quotation the report gives an explanation of the rearrangement of the bill and the object thereof:

> "The bill embodies a proposed *new arrangement for the income tax title.* The basis for the arrangement is the distribution of the provisions by *two*

classifications: General Provisions and Supplemental provisions. • • •

"The General Provisions are those which apply to the *ordinary transactions of the ordinary classes of taxpayers.* It is believed that 80 per centum of the taxpayers who file returns under the new Act will find in the General Provisions practically all of the income tax statute law of interest to them. The General Provisions are divided into parts.

"The Supplemental Provisions *are those* which apply only to extraordinary classes of taxpayers or which apply *only to the extraordinary transactions of ordinary classes of taxpayers.* The Supplemental Provisions are divided into Supplements." (Italics supplied.)

lso, see, to same effect, Committee on Finance Report No. 960, 70th Congress, 1st Session, p. 18.)

In enacting the Revenue Act of 1928, Congress legislated Table of Contents, divided into titles, subtitles, parts nd su plements, with section headings. It also entitled ach section of the Act.

When the Revenue Bill of 1932, H. R. 123, was reported o the House, the Ways and Means Committee stated Report No. 708, 72nd Congress, 1st Session):

"The proposed bill follows the general plan of the Revenue Act of 1928. The proposed income tax title is made applicable to 1932 and subsequent taxable years."

When the Committee on Finance reported the bill to he Senate, it made exactly the same statement. (Report o. 665, 72nd Congress, 1st Session.) The bill became the

Revenue Act of 1932 under the foregoing legislative representations. Like the Act of 1928, the 1932 Act had included within its provisions a Table of Contents, divided into titles, subtitles, parts and supplements, with section headings. The 1932 Act, therefore, has its General Provisions intended for the ordinary transactions of ordinary classes of taxpayers and *its Supplemental Provisions applying "to the extraordinary transactions of ordinary classes of taxpayers"*, which included section 115(c). The dissolution of a corporation may not be classed as an "ordinary transaction".

In Part II of Subtitle B we find a provision for "Computation of Net Income" under the heading "General Provisions". Part II contains the section 23 upon which petitioner wholly relies to claim additional tax in this case by subordinating section 115(c) to section 23(r)(1). Petitioner ignores or obscures the fact that section 23(r)(1) can be applied only to the *"ordinary transactions of the ordinary classes of taxpayers"*.

In Supplement B we also find a provision for "Computation of Net Income" under "Subtitle C—Supplemental Provisions". Under this Supplement B we find the sections 111, 112 and 115 which petitioner desires to substitute for section 23. Supplement B is the independent and complete provision for computing the net income for *"extraordinary transactions of ordinary classes of taxpayers"*.

The *"distributions in liquidation"* of corporations provided for in section 115(c) cannot be considered as the *"ordinary transactions"* of a corporation but, because the section falls within Supplement B, they *must* be consid-

ered as the *"extraordinary transactions"* of corporations. Such transactions are far different than the "sales or exchanges" of stock by shareholders as contemplated by section 23(r)(1). Therefore, the net income of respondent as effected by section 115(c) must be computed under that section and sections 111 and 112.

It thus becomes apparent why and how the authorities and legislative history relied upon by petitioner and referred to above have no application to the case at bar.

Petitioner argues (Brief pp. 14-18) that the legislative history of section 23(r)(1) does not support our contention that it is not applicable and quotes in part from the Committee Reports. (Brief pp. 16 and 17.) Reading petitioner's quotations with those found in respondent's brief (Appendix B, pp. iv-vi), or reading the entire reports, will disclose that nowhere is there any expression of intent to apply the words "sales or exchanges" beyond their ordinary meaning. Also, it is clear that Congress did not indicate, even by the most obscure reference, any intent to interfere with the separate method of computation of net income in "distributions by corporations" found in section 115(c) under Supplement B of Subtitle C of the Revenue Act of 1932. To have made subsection 23(r)(1) applicable to subsection 115(c), Congress would have been required to amend section 115(c) or enlarge the language of section 23(r)(1) so that it could be applicable to section 115(c)—this Congress did not do.

2. **THE LONG ACCEPTED MEANING OF "SALES OR EXCHANGES" DEFEATS PETITIONER'S CONTENTIONS.**

The legislative history does not support the petitioner's contention that "the long accepted meaning of the words" sales or exchanges "used in section 23(r)(1) makes unavailable reference to the legislative history of that section". (Brief, p. 14.) The legislative history shows no inclination to enlarge the meaning of "sales and exchanges", such as petitioner seeks to do. To the contrary, the legislative history distinctly shows that those words were used to stop a common practice of minimizing taxes within the ordinary usage of the words "sales or exchanges". This Court has pronounced the rule which petitioner seeks to evade, viz.:

> "Unless the contrary appears, statutory words are presumed to be used in their ordinary and necessary sense, with the meaning commonly attributable to them."
>
> *DeGanay v. Lederer*, 250 U. S. 376, 381.

The words "sales or exchanges", as used in section 23(r)(1) had "no long accepted meaning", other than their ordinary meaning, when inserted in the statute. That section had never been interpreted by Court or regulation and has not to this day been interpreted in any way excepting in this case and in *Davis v. United States*, 87 Fed. (2d) 323, 325, where the constitutionality of the section was involved. In upholding the section on the challenge of its conflict with Article I, section 9 and the Fifth Amendment of the Federal Constitution, the Court did so upon the sole ground that section 23(r)(1) was aimed only at "probable speculative income and losses".

That decision did not contemplate the words "sales or exchanges" being used in the extraordinary sense sought by petitioner.

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3. PETITIONER'S CONSTRUCTION DOES INVOLVE A HARSH AND ABSURD RESULT.

Petitioner's assertion to the contrary (Brief p. 18) is not supported by the facts. Its position is absurd for the following reasons:

(a) It seeks to ignore the method of "Computation of Net Income" as provided for in Supplement B of Subtitle C of the Revenue Act of 1932 and erase sections 111, 112 and 115 from the Act in order to make section 23(r)(1) applicable.

(b) It seeks to interpret an ordinary and willing transaction, such as a sale or exchange, into an unwilling transaction, such as the distributions in liquidation of a corporation.

Its position is harsh because it seeks to transpose the language of section 23(r)(1) into something with a meaning beyond the words used by Congress, and to interpret an unusual, and in this case unfortunate, proceeding as a device to avoid taxes.

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4. THE LOSS IS DEDUCTIBLE UNDER SECTIONS 115(c), 111 AND 112.

Petitioner attacks the decision of the Court below on the ground that the loss is not deductible under sections 22(d). 115(c), 111 and 112. (Brief, p. 20.)

Heretofore, under title 1 of this argument, we have shown the independence of sections 111, 112 and 115 for the computation of net income for extraordinary transactions of an ordinary class of taxpayer. Section 22(d), which falls within Part II of Subtitle B—General Provisions for the computation of net income, provides the emphasis on the inapplicability of section 23(r)(1). That subsection definitely provides that the only way in which shareholders of a corporation may be taxed upon distributions by corporations. By subsection 22(d) Congress in passing the Revenue Acts of 1928 and 1932 issued an ultimatum which section 23(r)(1) does not overcome. One has but to turn to sections 112 and 115 in the subsequent Revenue Acts of 1934, 1936 and 1938 to observe that Congress has amended those sections to overcome the shortcomings of Supplement B of Subtitle C rather than amend Part II of Subtitle B to make the General Provisions apply.

CONCLUSION.

The majority decision of the Court below should be sustained.

Dated, San Francisco, California,
November 9, 1938.

Respectfully submitted.

ADOLPHUS E. GRAUPNER,
ARTHUR E. COOLEY,
Counsel for Respondent.

SUPREME COURT OF THE UNITED STATES.

No. 304.—October Term, 1938.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, vs. Chester N. Weaver Company.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit.

[December 5, 1938.]

Mr. Justice Stone delivered the opinion of the Court.

The question to be decided is whether payments received by a corporation as a stockholder in another corporation, upon the latter's complete liquidation, are to be treated as payments upon a sale or exchange of the stock under § 23(r) (1) of the Revenue Act of 1932, 47 Stat. 169, which allows the deduction of losses from sales or exchanges of stock, not held for more than two years, only to the extent of the gains from such sales or exchanges.

On August 9, 1932, respondent, a California corporation, purchased shares of stock in another corporation. In the following year the latter was completely liquidated. The liquidating dividends received by respondent amounted to less than the cost of the stock. In its income tax return for 1933 respondent deducted the full amount of the loss from gross income. The commissioner ruled that, since the loss was sustained upon an exchange of stock held less than two years and the respondent had received no gains against which the loss could be applied, the deduction was forbidden by § 23(r)(1), and he found a deficiency accordingly. The order of the Board of Tax Appeals sustaining the deficiency was reversed by the Court of Appeals for the Ninth Circuit, 97 F. (2d) 31. We granted certiorari, — U. S. —, to resolve the conflict between the decision of the court below and that of the Court of Claims in *White* v. *United States*, 21 Fed. Supp. 361, this day affirmed on certiorari in Nos. 96 and 97, *White* v. *United States*.

Section 23(f) provides that losses sustained by corporations during the taxable year shall be allowed as deductions in computing

net income, subject to the limitations provided in sub-section (r). Sub-section (r) (1) declares:

"Losses from sales or exchanges of stocks and bonds . . . which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchanges . . . ." By § 101 "'Capital assets' means property held by the taxpayer for more than two years . . . ."

Since the loss sustained by respondent was not from the sale or exchange of the stock, it is contended that sub-section (r) has no application and that the loss is deductible in full, as are other losses, under § 23(f). Whether § 23(f) or 23(r) applies must be answered by deciding whether, under § 115(c), stockholders' losses upon a corporate liquidation are to be treated, for purposes of computation of the tax, in the same manner as losses upon a sale or exchange of the stock.

The scheme of the 1932 Act, as respects the treatment of gains and losses upon the sale or exchange of property on a different basis from other types of gain or loss, is substantially that of the 1928 Act, which we have considered in *White* v. *United States*, *supra*. The provisions of §§ 12(c), 22(d), (e), 23, 101, 111, 112, 113 and 115(c) of the 1928 Act, discussed in the *White* case, so far as now relevant were reenacted in the same numbered sections of the 1932 Act. The considerations which in that case led us to the conclusion that § 115(c) of the 1928 Act had placed stockholders' gains and losses from liquidations on the same basis as gains and losses from sales of the stock for purposes of computation of the tax, lead us to the same conclusion with respect to the 1932 Act.

We find nothing in the language or history of § 23(r) to suggest that Congress, in enacting it, had any purpose to restrict the operation of § 115(c) as we have construed it. Section 23(r), like § 101 in the 1932 and earlier Acts, speaks of losses resulting only from sales or exchanges. But the one does not more than the other restrict the operation of the provisions of §§ 115 and 112, which accord to losses on liquidation the same recognition accorded by § 23(r) to losses upon sales. Congress, in enacting the 1934 Act, recognized that under that of 1932 " . . . . a distribution in liquidation of a corporation is treated in the same manner as a sale of stock." Report of Senate Committee on Finance, No. 558, 73rd Cong., 2nd Sess., p. 37. To prevent avoidance of surtax through liquidation of corporations with large surpluses, Congress found it necessary to place gains on liquidations on a different basis from

gains on sales. It accomplished this by amending § 115(c) to provide: "Despite the provisions of section 117(a) [corresponding to § 101 in the earlier Acts specially taxing capital gains and losses] 100 per centum of the gain so recognized shall be taken into account in computing net income."

It follows that the extent to which the taxpayer can deduct the loss is controlled by § 23(r)(1), and that since the stock was held for less than two years and there were no gains against which the loss could be offset, it can not be deducted from gross income.

Reversed.

Mr. Justice McReynolds, Mr. Justice Butler and Mr. Justice Roberts dissent.

A true copy.

Test:

Clerk, Supreme Court, U. S.